COPART INC
Form 10-Q
December 11, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

x	**Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934** **for the quarterly period ended October 31, 2006**
	OR
o	**Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934** **for the transition period from to**

Commission file number: 0-23255

COPART, INC.

(Exact name of registrant as specified in its charter)

California (State or other jurisdiction of incorporation or organization)	**94-2867490** (I.R.S. Employer Identification Number)

4665 Business Center Drive, Fairfield, CA 94534
(Address of principal executive offices with zip code)

Registrant s telephone number, including area code: **(707) 639-5000**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES x NO o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer x Accelerated Filer o Non-Accelerated Filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES o NO x

Number of shares of Common Stock outstanding as of December 8, 2006: 90,579,975

Copart, Inc.

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October 31, 2006

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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Copart, Inc.

Consolidated Balance Sheets

(in thousands)

(Unaudited)

	October 31, 2006	July 31, 2006
ASSETS		
Current assets:		
Cash and cash equivalents	$ 126,645	$ 126,590
Short-term investments	187,055	148,725
Accounts receivable, net	100,375	99,959
Vehicle pooling costs	28,396	29,148
Income taxes receivable		2,064
Prepaid expenses and other assets	4,735	4,864
Total current assets	447,206	411,350
Property and equipment, net	348,218	341,943
Intangibles, net	1,690	1,874
Goodwill	112,291	112,291
Deferred income taxes	6,247	5,137
Land purchase options and other assets	23,375	22,110
Total assets	$ 939,027	$ 894,705
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities	$ 56,979	$ 60,644
Deferred revenue	14,372	15,372
Income taxes payable	15,482	
Deferred income taxes	6,959	7,191
Other current liabilities	126	126
Total current liabilities	93,918	83,333
Other liabilities	1,434	1,402
Total liabilities	95,352	84,735
Commitments and contingencies		
Shareholders equity:		
Common stock, no par value - 180,000 shares authorized; 90,554 and 90,445 shares issued and outstanding at October 31, 2006 and July 31, 2006, respectively	279,053	276,052
Accumulated other comprehensive income (loss)	322	(37)
Retained earnings	564,300	533,955
Total shareholders equity	843,675	809,970
Total liabilities and shareholders equity	$ 939,027	$ 894,705

See accompanying notes to consolidated financial statements.

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Copart, Inc.

Consolidated Statements of Income

(in thousands except per share amounts)

(Unaudited)

	Three months ended October 31, 2006	2005
Revenues	$ 132,121	$ 116,739
Operating costs and expenses:		
Yard operations	70,231	69,207
General and administrative	14,997	13,533
Total operating expenses	85,228	82,740
Operating income	46,893	33,999
Other income (expense):		
Interest income, net	3,027	1,775
Other income	651	638
Equity in losses of unconsolidated entity	(2,216)	
Total other income	1,462	2,413
Income from continuing operations before income taxes	48,355	36,412
Income taxes	18,010	13,746
Income from continuing operations	30,345	22,666
Discontinued operations:		
Income from discontinued operations, net of income tax effects		147
Net Income	$ 30,345	$ 22,813
Earnings per share-basic		
Income from continuing operations	$ 0.34	$ 0.25
Income from discontinued operations		
Basic net income per share	$ 0.34	$ 0.25
Weighted average shares outstanding	90,500	90,385
Earnings per share-diluted		
Income from continuing operations	$ 0.32	$ 0.24
Income from discontinued operations		0.01
Diluted net income per share	$ 0.32	$ 0.25
Weighted average shares and dilutive potential common shares outstanding	93,375	92,730

See accompanying notes to consolidated financial statements.

Copart, Inc.

Consolidated Statements of Cash Flows

(in thousands)

(Unaudited)

	Three Months Ended October 31,	
	2006	**2005**
Cash flows from operating activities:		
Net income	$ 30,345	$ 22,813
Adjustments to reconcile net income to net cash provided by operating activities:		
Income from discontinued operations		(593)
Depreciation and amortization	8,740	7,109
Allowance for doubtful accounts	(37)	380
Deferred rent	32	(66)
Share-based compensation	848	723
Loss on sale of property and equipment	38	40
Deferred income taxes	(1,342)	(1,405)
Equity in loss of unconsolidated entity	2,216	
Changes in operating assets and liabilities, net of effects from acquisitions:		
Accounts receivable	(379)	(3,306)
Vehicle pooling costs	752	(3,839)
Prepaid expenses and other current assets	190	(35)
Other assets	(296)	(2,101)
Accounts payable and accrued liabilities	(3,665)	(475)
Deferred revenue	(1,000)	2,514
Income taxes receivable	2,064	
Income taxes payable	15,482	8,250
Net cash provided by operating activities from continuing operations	53,988	30,009
Net cash provided by operating activities from discontinued operations		356
Net cash provided by operating activities	53,988	30,365
Cash flows from investing activities:		
Purchases of short-term investments	(213,800)	(263,380)
Sales of short-term investments	175,470	113,660
Purchases of property and equipment	(21,102)	(23,523)
Proceeds from sale of property and equipment	3,013	252
Purchases of goodwill, intangibles, property, equipment and net current assets in connection with acquisitions		(3,348)
Investment in unconsolidated entity		(3,000)
Net cash used in investing activities from continuing operations	(56,419)	(179,339)
Net cash used in investing activities from discontinued operations		(2)
Net cash used in investing activities	(56,419)	(179,341)
Cash flows from financing activities:		
Proceeds from the exercise of stock options	1,570	1,710
Proceeds from the issuance of Employee Stock Purchase Plan shares	7	
Excess tax benefit from share-based payment arrangements	576	519
Net cash provided by financing activities from continuing operations	2,153	2,229
Net cash provided by financing activities from discontinued operations		
Net cash provided by financing activities	2,153	2,229

Effect of foreign currency translation	333	(33)
Net increase (decrease) in cash and cash equivalents	55	(146,780)
Cash and cash equivalents at beginning of period	126,590	252,548
Cash and cash equivalents at end of period	$ 126,645	$ 105,768
Supplemental disclosure of cash flow information:		
Income taxes paid	$ 1,388	$ 6,668

See accompanying notes to consolidated financial statements.

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Copart, Inc.

Notes to Consolidated Financial Statements

October 31, 2006

(Unaudited)

NOTE 1 Business and Basis of Presentation

Description of Business

Copart, Inc. and its subsidiaries (collectively, the Company) provide vehicle suppliers, primarily insurance companies, with a full range of services to process and sell salvage vehicles over the Internet through the Company s Virtual Bidding Second Generation (VB2) Internet auction-style sales technology. The Company sells principally to licensed vehicle dismantlers, rebuilders, repair licensees, used vehicle dealers and exporters. Salvage vehicles are either damaged vehicles deemed a total loss for insurance or business purposes or are recovered stolen vehicles for which an insurance settlement with the vehicle owner has already been made. The Company offers vehicle suppliers a full range of services that expedite each stage of the salvage vehicle sales process and minimize administrative and processing costs.

Principles of Consolidation

In the opinion of the management of the Company, the accompanying unaudited consolidated financial statements contain all adjustments (which are normal recurring accruals) necessary to present fairly its financial position as of October 31, 2006 and July 31, 2006, and its consolidated statements of income and cash flows for the three months ended October 31, 2006 and October 31, 2005. Interim results for the three months ended October 31, 2006 are not necessarily indicative of the results that may be expected for the year ending July 31, 2007. The interim financial statements should be read in conjunction with the Company s Annual Report on Form 10-K for the fiscal year ended July 31, 2006.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and reported consolidated results of operations during the reporting period. Estimates are used for, but not limited to, vehicle pooling costs, self-insured reserves, allowance for doubtful accounts, goodwill, income taxes, revenue recognition, share-based compensation and long-lived assets. Actual results could differ from those estimates.

Income Taxes

Income taxes are accounted for under the asset and liability method. 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 bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Reclassifications

Certain prior year amounts have been classified to conform to the current year presentation.

NOTE 2 Vehicle Pooling Costs

The Company defers, in vehicle pooling costs, certain yard and fleet expenses associated with vehicles consigned to and received by us but not sold as of the balance sheet date. The Company quantifies the deferred costs using a calculation that includes the number of vehicles at its facilities at the beginning and end of the period, the number of vehicles sold during the period and an allocation of certain yard and fleet expenses of the period. The primary expenses allocated and deferred are certain facility costs, labor, transportation, and vehicle processing. If its allocation factors change, then yard and fleet expenses could increase or decrease correspondingly in the future. These costs are expensed as vehicles are sold in the subsequent periods on an average cost basis.

The operating results for the first quarters of fiscal 2007 and fiscal 2006 were adversely affected by incremental costs, characterized as abnormal in Financial Accounting Standards (FAS) 151: Inventory Costs, incurred as a result of Hurricanes Katrina and Rita. These additional inventory-type costs, characterized as abnormal and charged to yard operations costs, are approximately $0.4 million and $4.6 million for the three month periods ended October 31, 2006 and October 31, 2005, respectively. These costs include

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the additional subhauling, payroll, equipment and facilities expenses directly related to the operating conditions created by the hurricanes and will continue. These costs do not include normal expenses associated with the increased unit volume created by the hurricanes, which are deferred until the sale of the units and are recognized as vehicle pooling costs on the balance sheet. At the end of October 31, 2006, approximately 10.6% of the incremental salvage vehicles received as a result of the hurricanes remained unsold and in inventory. The Company expects the majority of these vehicles to be sold primarily in the next quarter, provided that the Gulf Coast region does not experience additional hurricanes or severe weather. The processing of the hurricane vehicles has had and may continue to have a negative impact on gross and operating margin percentages.

NOTE 3 Net Income Per Share

There were no adjustments to net income in calculating diluted net income per share. The table below reconciles basic weighted shares outstanding to diluted weighted average shares outstanding (in thousands):

	Three months ended October 31,	
	2006	**2005**
Basic weighted average shares outstanding	90,500	90,385
Effect of dilutive securities stock options	2,875	2,345
Diluted weighted average shares outstanding	93,375	92,730

Options to purchase 5,000 and 883,500 shares of common stock at a weighted average price of $28.31 and $24.03 per share were outstanding during the quarters ended October 31, 2006 and 2005, respectively, but were not included in the computation of diluted earnings per share because the options exercise price was greater than the average market price of the common shares.

NOTE 4 - Short-term Investments

Short-term investments consist primarily of AAA-rated auction rate securities with readily determinable fair market values and with original maturities in excess of three months. Auction rate securities are principally variable rate securities tied to short-term interest rates. Auction rate securities have interest rate resets through a modified Dutch auction, at predetermined short-term intervals, usually every 7, 28 or 35 days. They trade at par and are callable at par on any interest payment date at the option of the issuer. Interest paid during a given period is based upon the interest rate determined during the prior auction. Although these instruments are issued and rated as long-term securities, they are priced and traded as short-term securities because of the liquidity provided through the interest rate reset.

The Company has classified its entire investment portfolio as available-for-sale. The Company views its available-for-sale securities as available for use in its current operations. Accordingly, the Company has classified all investments as short-term, even though the stated maturity may be one year or more beyond the current balance sheet date. Available-for-sale securities are reported at fair value, with unrealized gains and losses reported as a component of Shareholders Equity and Comprehensive Income. Unrealized losses are charged against income when a decline in the fair market value of an individual security is determined to be other than temporary. Realized gains and losses on investments are included in interest income.

Short-term investments consist of the following (in thousands):

	October 31, 2006	**July 31, 2006**
Available-for-sale securities:		
Auction rate securities	$ 187,055	$ 148,725
Total short-term investments	$ 187,055	$ 148,725

NOTE 5 Discontinued Operations and Goodwill Impairment

In the second quarter of fiscal 2006, the Company adopted a formal plan to discontinue the operations of its public auction business Motors Auction Group (MAG) and dispose of or convert the related assets. As of July 31, 2006, no MAG locations remained. The three month period ending October 31, 2005, has been restated to present the results for these operations as discontinued operations

Summarized results of operations for MAG is set forth below (in thousands):

	Three months ended October 31, 2005
Net revenue	$ 2,286
Income before income taxes	236
Income tax expense	(89)
Net income from discontinued operations	$ 147

NOTE 6 Goodwill and Intangible Assets

The following table sets forth intangible assets by major asset class as of the dates indicated (in thousands):

	October 31, 2006	July 31, 2006
Amortized intangibles:		
Covenants not to compete	$ 10,071	$ 10,071
Accumulated amortization	(8,381)	(8,197)
Net intangibles	$ 1,690	$ 1,874

Aggregate amortization expense on intangible assets was $0.2 million for the three months ended October 31, 2006 and 2005, respectively. The average life of the covenants not to compete is approximately five years. Estimated amortization expense for each of the five succeeding fiscal years is as follows (in thousands):

2007 (nine months remaining)	$ 616
2008	410
2009	309
2010	296
2011	47
Thereafter	12
Total	$ 1,690

The change in the carrying amount of goodwill is as follows (in thousands):

Balance as of July 31, 2006	$	112,291
Goodwill acquired during the period		
Balance as of October 31, 2006	$	112,291

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NOTE 7 Share-Based Compensation

Effective August 1, 2005, the Company adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), Share-Based Payment (SFAS 123(R)), requiring it to recognize expense related to the fair value of its share-based compensation awards. The Company elected to use the modified prospective transition method as permitted by SFAS 123(R). Under this transition method, share-based compensation expense for the three months ended October 31, 2006 and October 31, 2005, includes compensation expense for all share-based compensation awards granted prior to, but not yet vested as of August 1, 2005, based on the grant-date fair value estimated in accordance with the original provisions of SFAS 123 Accounting for Stock-Based Compensation , net of estimated forfeitures. Share-based compensation expense for all stock-based compensation awards granted subsequent to August 1, 2005 was based on the grant-date fair value estimated in accordance with the provisions of SFAS 123(R). For options issued subsequent to August 1, 2005, the Company recognizes compensation expense for stock option awards on a straight-line basis over the requisite service period of the award. For options issued prior to August 1, 2005, the Company recognizes compensation expense for stock option awards on a graded vesting basis over the requisite service period of the award.

The following is a summary of option activity for the Company s stock option plans:

	Shares (in 000s)	**Weighted-average Exercise Price**	**Weighted-average Remaining Contractual Term**	**Aggregate Intrinsic Value (in 000s)**
Outstanding at July 31, 2006	5,878	$ 12.80		
Grants of options	71	$ 26.75		
Exercises	(111)	$ 14.70		
Forfeitures or expirations	(6)	$ 21.58		
Outstanding at October 31, 2006	5,832	$ 12.93	5.16	$ 93,838
Exercisable at October 31, 2006	4,434	$ 10.69	4.20	$ 80,889

The aggregate intrinsic value is calculated as the difference between the exercise price of the underlying awards and the quoted price of the Company s common stock for the 5,858,441 options that were in-the-money at October 31, 2006.

NOTE 8 Common Stock Repurchases

In February 2003, the Company s Board of Directors authorized the Company to repurchase up to 9.0 million shares of its common stock. The repurchases may be effected through solicited or unsolicited transactions in the open market or in privately negotiated transactions. No time limit has been placed on the duration of the share repurchase program. The repurchases will be made at such times and in such amounts as the Company deems appropriate and may be discontinued at any time. The Company did not repurchase any shares during the three months ended October 31, 2006. The total number of shares repurchased under the program as of October 31, 2006 is approximately 4.0 million, leaving approximately 5.0 million available under the repurchase program.

NOTE 9 Segment Reporting

The Company operates in a single segment providing vehicle suppliers, primarily insurance companies, with a full range of services to process and sell salvage vehicles over the Internet through its Virtual Bidding Second Generation (VB2) Internet auction-style sales technology.

NOTE 10 Comprehensive Income

The following table reconciles net income to comprehensive income (in thousands):

	Three months ended October 31, 2006	**2005**
Net income, as reported	$ 30,345	$ 22,813
Other comprehensive income:		
Foreign currency translation adjustments, net of tax	359	14

Total other comprehensive income	$	30,704	$	22,827

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NOTE 11 Recent Accounting Pronouncements

In September 2006, the SEC issued SAB No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements* (SAB No. 108) to provide guidance on the consideration of the effects of prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. Under SAB No. 108, companies should evaluate a misstatement based on its impact on the current year income statement, as well as the cumulative effect of correcting such misstatements that existed in prior years existing in the current year s ending balance sheet. SAB No. 108 will become effective for the Company in its fiscal year ending July 31, 2007. The Company is currently evaluating the impact of the provisions of SAB No. 108 on its financial statements.

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement No. 157, *Fair Value Measurements* (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. FAS 157 is effective for fiscal years beginning after November 15, 2007. The Company is currently assessing the potential impact on our financial statements.

NOTE 12 Equity Investment and Related Party Transaction

During the three months ended October 31, 2005, the Company committed to invest $9.0 million for a 50% equity interest in Lanelogic, LLC, a Delaware limited liability Company (Lanelogic), of which $3.0 million was contributed during the three months ended October 31, 2005 and $6.0 million was contributed during the three months ended January 31, 2006. The Company has no further contractual funding commitment. Based on the Company s evaluation of Lanelogic and related agreements, management believes Lanelogic does not constitute a Variable Interest Entity as defined in FASB Interpretation No.46, Consolidation of Variable Interest Entities . As a result, the Company s investment has been accounted for under the equity method prescribed by Accounting Principles Board Opinion No. 18, The Equity Method of Accounting for Investments in Common Stock .

Lanelogic is in the process of recapitalization and is seeking additional equity financing. Due to the timing of the closing of any possible transaction, the Company s Chairman and CEO, subsequent to the end of the first quarter of fiscal 2007 made a personal unsecured loan to Lanelogic to prevent a restriction of working capital from disrupting its roll out. While the Company is currently evaluating the accounting implications of this loan, if, by making the loan, the Company is deemed to control Lanelogic for accounting purposes, then beginning in the second quarter of fiscal 2007 and for as long as the Company is considered to exercise control, the Company will consolidate Lanelogic s results with its results and its recognizable losses will no longer be limited to the amount of its investment. However, the Company is not obligated or otherwise required to contribute any additional cash to Lanelogic.

NOTE 13 Legal Proceedings

The Company is involved in litigation and damage claims arising in the ordinary course of business, such as actions related to injuries, property damage, and handling or disposal of vehicles. This litigation includes the following matters:

Ciano Dessources filed a lawsuit on May 21, 2003, in the Commonwealth of Massachusetts, Superior Court Department against Copart of Connecticut, Inc. and Copart, Inc., which purported to be a class action on behalf of persons whose vehicles were disposed of by the Company as abandoned vehicles and which the named plaintiff contends were disposed of without complying with state laws. Relief sought includes class certification, declaratory, remedial and/or injunctive relief, including the ordering of a compliance program that will essentially protect consumers, as well as damages, fees, and costs. Copart s motion for summary judgment was granted on December 8, 2004, dismissing the class claim element of the lawsuit. On August 9, 2006, Plaintiff s motion for summary judgment was denied. A trial date has been set for March 5, 2007. The Company believes the claim is without merit, and is defending the lawsuit vigorously.

On September 16, 2005, Richard M. Gray filed suit against Copart and A. Safrin in the State Court for the County of Chatham, State of Georgia, alleging a class action for unreasonable amounts claimed for storage liens by the Company, and related claims. Relief sought includes class certification, damages, fees, costs and expenses. The Company s motion for summary judgment was heard on December 4, 2006 and no decision has yet been made. The Company believes the claim is without merit, and is defending the lawsuit vigorously.

On July 28, 2006, Foreign Car Sales and Service LLC filed suit against Copart in the United States District Court for the Middle District of Louisiana alleging antitrust violations and unfair trade practices. Relief sought includes class certification, damages, fees, costs and expenses. Plaintiff is in pro per and is demanding a total award of the now current value of 51% of the Company s issued stock. The Company believes the claim is without merit, and is defending the lawsuit vigorously.

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On August 7, 2006, Kimberly and Jason Green filed suit against Copart in the Superior Court of the State of California, County of Sacramento, making allegations pursuant to a California consumer protection statute similar to a class action for unreasonable amounts claimed for storage liens by the Company, and related claims. Relief sought includes class certification, damages, fees, costs and expenses. The Company filed an answer on September 1, 2006 denying the claim. The Company believes the claim is without merit, and is defending the lawsuit vigorously.

The Company provides for costs relating to these matters when a loss is probable and the amount can be reasonably estimated. The effect of the outcome of these matters on the Company s future results of operations cannot be predicted because any such effect depends on future results of operations and the amount and timing of the resolution of such matters. The Company believes that any ultimate liability will not have a material effect on its financial position, results of operations or cash flows. However, the amount of the liabilities associated with these claims, if any, cannot be determined with certainty.

ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This report, including the information incorporated by reference herein, contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. All statements other than statements of historical facts are statements that could be deemed forward-looking statements. In some cases, you can identify forward-looking statements by terms such as may, will, should, expect, plan, intend, forecast, anticipate, believe, estimate, predict, potential, continue or the negative of these terms or other comparable terminology. The forward-looking statements contained in this report involve known and unknown risks, uncertainties and situations that may cause our or our industry s actual results, level of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these statements. These factors include those listed in Part II, Item 1A Risk Factors beginning on page 20 of this report and those discussed elsewhere in this report. We encourage investors to review these factors carefully.

Although we believe that, based on information currently available to the Company and its management, the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. You should not place undue reliance on these forward-looking statements and we undertake no obligation to revise or update any forward-looking statements for any reason.

Overview

We provide vehicle suppliers, primarily insurance companies, with a full range of services to process and sell salvage vehicles over the Internet through our Virtual Bidding Second Generation (VB2) Internet auction-style sales technology. We sell principally to licensed vehicle dismantlers, rebuilders, repair licensees, used vehicle dealers and exporters. Salvage vehicles are either damaged vehicles deemed a total loss for insurance or business purposes or are recovered stolen vehicles for which an insurance settlement with the vehicle owner has already been made. We offer vehicle suppliers a full range of services that expedite each stage of the salvage vehicle sales process and minimize administrative and processing costs. We generate revenues primarily from fees paid by vehicle suppliers and vehicle buyers, as well as related fees for services such as towing and storage.

At the election of the vehicle supplier, we sell vehicles pursuant to our Percentage Incentive Program (PIP) consignment basis or on a fixed fee consignment basis. Under the PIP program, we agree to sell all of the salvage vehicles of a vehicle supplier in a specified market usually for a predetermined percentage of the vehicle sales price. Under our fixed fee consignment program, we sell vehicles for a fixed consignment fee. Although sometimes included in the consignment fee, we may also charge additional fees for the cost of transporting the vehicle to our facility, storage of the vehicle, and other incidental costs. Using either consignment method, only the fees associated with vehicle processing are recorded in revenue, not the actual sales price (gross proceeds).

Our revenues consist of salvage fees charged to vehicle suppliers and vehicle buyers, transportation revenue and purchased vehicle revenues. Salvage fees from vehicle suppliers include sales fees under PIP agreements and fixed fee programs where we charge for title processing, special preparation, storage and selling. Salvage fees also include fees charged to vehicle buyers for purchasing vehicles, storage and annual registration. Transportation revenue includes charges to suppliers for towing vehicles under certain contracts. Transportation revenue also includes towing charges assessed to buyers for delivering vehicles. Purchased vehicle revenues are comprised of the price that buyers paid for vehicles that we own.

Costs attributable to yard operations consist primarily of operating personnel (which includes yard management, clerical and yard employees), rent, contract vehicle towing, insurance, fuel, equipment maintenance and repair, and costs of vehicles we sold under purchase contracts. Costs associated with general and administrative expenses consist primarily of executive management, accounting, data processing, sales personnel, human resources, professional fees, research and development and marketing expenses.

During fiscal 2004, we converted all of our salvage vehicle auction facilities to an Internet-based auction-style model using our VB2 Internet sales technology. This process employs a two-step bidding process. The first step, called the preliminary bid, allows buyers to submit bids up to one hour before a real time virtual auction begins. The second step allows buyers to bid against each other, and the high bidder from the preliminary bidding process, in a real-time process over the Internet.

During the second quarter of the fiscal year ending July 31, 2006, we adopted a formal plan to discontinue the operations of our public auction business Motors Auction Group (MAG) and dispose of or convert the related assets. The MAG yards converted into salvage facilities will continue to be included in the results of continuing operations on our income statements.

The period-to-period comparability of our operating results and financial condition is substantially affected by business acquisitions, new openings, weather and product introductions during such periods.

Acquisitions and New Operations

We have experienced significant growth as we have acquired nine vehicle storage facilities and established eleven new facilities since the beginning of fiscal 2005. All of these acquisitions have been accounted for using the purchase method of accounting.

As part of our overall expansion strategy of offering integrated services to vehicle suppliers, we anticipate acquiring and developing facilities in new regions, as well as the regions currently served by our facilities. As part of this strategy, in fiscal 2007 we opened a new facility in Baltimore, MD. In fiscal 2006 we acquired new facilities in or near Greenwood, Nebraska; Grand Island, Nebraska; York Haven, Pennsylvania; Chambersburg, Pennsylvania; Altoona, Pennsylvania; Fruitland, Maryland; Billings, Montana and opened new facilities in or near Honolulu, Hawaii; Lansing, Michigan; Dover, Florida and Jacksonville, Florida. In fiscal 2005 we acquired new facilities in or near Lexington, Kentucky and Columbia, Missouri and opened new facilities in Strongsville, Ohio; Ocala, Florida; Knoxville, Tennessee; Loganville, Georgia; Spokane, Washington; Tallahassee, Florida and Hialeah, Florida. We believe that these acquisitions and openings strengthen our coverage as we have 123 facilities located in North America and are able to provide national coverage for our suppliers.

We seek to increase revenues and profitability by, among other things, (i) acquiring and developing new salvage vehicle storage facilities in key markets, (ii) pursuing national and regional vehicle supply agreements, (iii) expanding our service offerings to suppliers and buyers, and (iv) expanding the application of VB2 into new markets. In addition, we implement our pricing structure and merchandising procedures and attempt to effect cost efficiencies at each of our acquired facilities by implementing our operational procedures, integrating our management information systems and redeploying personnel, when necessary.

Critical Accounting Policies and Estimates

The preparation of consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and the related disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates, including those related to vehicle pooling costs, allowance for doubtful accounts, goodwill, income taxes, long-lived assets and self insured liabilities. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Management has discussed the selection of critical accounting policies and estimates with the Audit Committee of the Board of Directors and the Audit Committee has reviewed our disclosure relating to critical accounting policies and estimates in this quarterly report on Form 10-Q. The following is a summary of the more significant judgments and estimates used in the preparation of our consolidated financial statements:

Revenue Recognition

We provide a portfolio of services to our sellers and buyers that facilitate the sale and delivery of a vehicle from seller to buyer. These services include the ability to use our VB2 Internet sales technology and vehicle delivery, loading, title processing, preparation and storage. We evaluate multiple-element arrangements relative to our buyer and seller agreements in accordance with Emerging Issues Task Force Issue No. 00-21, *Revenue Arrangements with Multiple Deliverables* (EITF 00-21), which addresses accounting for multiple-element arrangements, and Staff Accounting Bulletin No. 104, *Revenue Recognition* (SAB104), which addresses revenue recognition for units of accounting.

The services we provide to the seller of a vehicle involve disposing of a vehicle on the seller s behalf and under most of our current contracts, collecting the proceeds from the buyer. We are not entitled to any such seller fees until we have collected the sales proceeds from the buyer for the seller and, accordingly, we recognize revenue for seller services after service delivery and cash collection.

In certain cases, seller fees are not contingent upon collection of the seller proceeds from the buyer. However, we determined that we are not able to separate the services into separate units of accounting because we do not have fair value for undelivered items. As a result, we do not recognize seller fees until the final seller service has been delivered, which generally occurs upon collection of the sales proceeds from the buyer for the seller.

We provide a number of services to the buyer of the vehicle, charging a separate fee for each service. Each of these services has been assessed under the criteria of EITF 00-21 to determine whether we have met the requirements to separate them into units of accounting within a multi-element arrangement. We have concluded that the auction service and the post-auction services are separate units of accounting. The fees for the auction service are recognized upon completion of the auction, and the fees for the post-auction services are recognized upon successful completion of those services using the residual method.

We also charge buyers an annual registration fee for the right to participate in our vehicle sales program, which is recognized ratably over the term of the arrangement, and relist and late-payment fees, which are recognized upon receipt of payment by the buyer. No provision for returns has been established, as all sales are final with no right of return, although we provide for bad debt expense in the case of non-performance by our buyers and sellers.

Vehicle Pooling Costs

We defer, in vehicle pooling costs, certain yard operation expenses associated with vehicles consigned to and received by us but not sold as of the balance sheet date. We quantify the deferred costs using a calculation that includes the number of vehicles at our facilities at the beginning and end of the period, the number of vehicles sold during the period and an allocation of certain yard operation expenses of the period. The primary expenses allocated and deferred are certain facility costs, labor, transportation, and vehicle processing. If our allocation factors change, then yard operation expenses could increase or decrease correspondingly in the future. These costs are expensed as vehicles are sold in the subsequent periods on an average cost basis.

We apply the provisions of Statement of Financial Accounting Standards No. 151, *Inventory Costs* (SFAS 151) to our vehicle pooling costs. SFAS 151 requires that items such as idle facility expense, excessive spoilage, double freight and rehandling costs be recognized as current-period charges regardless of whether they meet the criteria of so abnormal as provided in Accounting Research Bulletin No. 43, Chapter 4, Inventory Pricing. In addition, SFAS 151 requires that the allocation of fixed production overheads to the costs of conversion be based on the normal capacity of production facilities. The adoption of SFAS 151 significantly increased yard expenses during fiscal 2006, as the Company incurred additional subhauling, payroll, equipment and facilities costs associated with Hurricanes Katrina and Rita.

Allowance for Doubtful Accounts

We maintain an allowance for doubtful accounts in order to provide for estimated losses resulting from disputed amounts billed to suppliers or buyers and the inability of our suppliers or buyers to make required payments. If billing disputes exceed expectations and/or if the financial condition of our suppliers or buyers were to deteriorate, additional allowances may be required.

Valuation of Goodwill and Intangibles

We evaluate the impairment of goodwill of our salvage sales operating segment, annually (or on an interim basis if certain indicators are present) by comparing the fair value of the operating segment to its carrying value. Future adverse changes in market conditions or poor operating results of the operating segment could result in an inability to recover the carrying value of the investment, thereby requiring impairment charges in the future.

Income Taxes and Deferred Tax Assets

We are also required to estimate income tax provisions and amounts ultimately payable or recoverable in numerous jurisdictions. Such estimates involve significant interpretations of regulations and are inherently very complex. Resolution of income tax treatments in individual jurisdictions may not be known for many years after completion of any fiscal year.

We also evaluate the realizability of our deferred tax assets on an ongoing basis. Generally accepted accounting principles require the assessment of the Company s performance and other relevant factors when determining the need for a valuation allowance with respect to these deferred tax assets. The Company s ability to realize deferred tax assets is dependent on its ability to generate future taxable income. Accordingly, the Company has established a valuation allowance when, in certain taxable jurisdictions, the utilization of the tax asset is uncertain. Additional timing differences, future earning trends and/or tax strategies may occur which could warrant a need for establishing an additional valuation allowance or a reserve.

Long-lived Asset Valuation

We evaluate long-lived assets and certain identifiable intangibles for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the estimated undiscounted cash flows change in the future, we may be required to reduce the carrying amount of an asset.

Share-Based Compensation

We account for our stock-based awards to employees and non-employees using the fair value method as required by SFAS No. 123(R), Share-Based Payment . SFAS No. 123(R) requires that the compensation cost related to share-based payment transactions, measured based on the fair value of the equity or liability instruments issued, be recognized in the financial statements. Determining the fair value of options using the Black-Scholes model, or other currently accepted option valuation models, requires highly subjective assumptions, including future stock price volatility and expected time until exercise, which greatly affect the calculated fair value on the grant date. If actual results are not consistent with the Company s assumptions and judgments used in estimating the key assumptions, the Company may be required to record additional compensation or income tax expense, which could have a material impact on financial position and results of operations.

Retained Insurance Liabilities

We are partially self-insured for certain losses related to medical, general liability, workers compensation and auto liability. Our liability represents an estimate of the ultimate cost of claims incurred as of the balance sheet date. The estimated liability is not discounted and is established based upon analysis of historical data and actuarial estimates. While we believe these estimates are reasonable based on the information currently available, if actual trends, including the severity of claims and medical cost inflation, differ from our estimates, our financial position, results of operations or cash flows could be impacted.

Results of Operations

Three Months Ended October 31, 2006 Compared to Three Months Ended October 31, 2005

Revenues from continuing operations were approximately $132.1 million during the three months ended October 31, 2006, an increase of approximately $15.4 million, or 13.2%, over the three months ended October 31, 2005. The increase was due to increased vehicle sales volume and increased revenue per transaction, which was driven by increased auction proceeds per vehicle. The increase in unit volume was driven by the additional salvage vehicles associated with Hurricanes Katrina and Rita, growth in vehicles processed at existing yards and vehicles processed from new yards opened or acquired in fiscal 2006. The increase in gross proceeds per vehicle (the gross sales price of the vehicle at auction) yields higher revenue per car as buyer fees and certain seller fees, including those sold under the PIP program, are based on the gross proceeds per vehicle and generally increase as gross proceeds per vehicle grow. We believe the increase in recent periods in proceeds per vehicle has been largely attributable to VB2, which allows more buyers to participate in the auctions. Given that VB2 has now been implemented across all of our yards for approximately two years, we do not expect to continue to experience the same incremental favorable impact from VB2 that we have experienced in prior periods. Existing facilities contributed approximately $12.5 million of the revenue growth and new facilities in or near York Haven, Pennsylvania; Chambersburg, Pennsylvania; Altoona, Pennsylvania; Fruitland, Maryland; Lansing, Michigan; Billings, Montana; Dover, Florida and Jacksonville, Florida contributed approximately $2.9 million of new revenue growth.

Yard operation expenses from continuing operations were approximately $70.2 million during the three months ended October 31, 2006, an increase of approximately $1.0 million, or 1.5%, over the three months ended October 31, 2005. Included in yard expenses is depreciation expense of $7.5 million, an increase of $1.4 million over fiscal 2005. Yard operation expenses decreased to 53.2% of revenues during three months ended October 31, 2006, as compared to 59.3% of revenues during the three months ended October 31, 2005. The decreases in yard expenses, excluding depreciation, were primarily attributable to the decrease in incremental abnormal costs incurred as a result of Hurricanes Katrina and Rita during the three months ended October 31, 2005. These additional inventory-type costs were approximately $4.6 million during the three months ended October 31, 2005 as compared to $0.4 million during the three months ended October 31, 2006, and were charged to yard operations in accordance with SFAS 151. These costs include the additional subhauling, payroll, equipment and facilities expenses directly related to the operating conditions created by the hurricanes. These costs do not include normal expenses associated with the increased unit volume created by the hurricanes, which are deferred until the sale of the units and are recognized as vehicle pooling costs on the balance sheet. At the end of the quarter, approximately 10.6% of the incremental salvage vehicles received as a result of the hurricanes remained unsold and in inventory. We expect the majority of these vehicles to be disposed primarily in the second quarter of fiscal 2007. If the Gulf Coast region were to experience additional adverse weather conditions during the next quarter, we may be unable to sell the existing vehicles within the currently anticipated time frame, which may have an adverse effect on our operating results. The processing of these vehicles has had and may continue to have a negative impact on gross and operating margin percentages.

General and administrative expenses from continuing operations were approximately $15.0 million for the three months ended October 31, 2006, an increase of approximately $1.5 million, or 10.8%, over the three months ended October 31, 2005. The increase was primarily due to increases in information technology payroll costs, costs relating to Sarbanes-Oxley compliance, SFAS 123(R) stock compensation costs and outside legal expense and general corporate expansion. General and administrative expenses decreased slightly to 11.4% of revenues during the three months ended October 31, 2006, as compared to 11.6% of revenues during fiscal 2005.

Total other income was approximately $1.5 million during the three months ended October 31, 2006, a decrease of approximately $0.9 million from the three months ended October 31, 2005. The decrease was due primarily to a $2.2 million loss recognized from an equity investment in Lanelogic LLC, a Delaware limited liability company (Lanelogic). Lanelogic is in the process of recapitalization and is seeking additional equity financing. Due to the timing of the closing of any possible transaction, our Chairman and CEO, subsequent to the end of the first quarter of fiscal 2007 made a personal unsecured loan to Lanelogic to prevent a restriction of working capital from disrupting its roll out. While we are evaluating the accounting implications of this loan, if, by making the loan, we are deemed to control Lanelogic for accounting purposes, then beginning in the second quarter of fiscal 2007 and for as long as we are considered to exercise control, we will consolidate Lanelogic s results with our results and our recognizable losses will no longer be limited to the amount of our investment. However, we are not obligated or otherwise required to contribute any additional cash to Lanelogic. This loss was offset by an increase in interest income of approximately $3.0 million due to higher interest rates and a higher average cash and investments balance.

Our effective combined federal, state and local income tax rates for three months ended October 31, 2006 and 2005 were approximately 37.2% and 37.8%, respectively. The decrease in the effective tax rate is primarily the result of adjustments to our state tax reserves based on the favorable outcome of an audit.

Due to the foregoing factors, we realized net income of approximately $30.3 million for the three months ended October 31, 2006, compared to net income of approximately $22.8 million for the three months ended October 31, 2005.

Liquidity and Capital Resources

Historically, we have financed our growth through cash generated from operations, public offerings of common stock, the equity issued in conjunction with certain acquisitions and debt financing. Cash and cash equivalents, combined with short-term investments increased by approximately $38.4 million from July 31, 2006 to October 31, 2006, as a result of cash generated from continuing operations, which was reduced by cash used for purchases of property and equipment. During the winter months, most of our facilities process 10% to 30% more vehicles than at other times of the year. This increased seasonal volume requires the increased use of our cash to pay out advances and handling costs of the additional business. Our primary source of cash generated by operations is from the collection of sellers fees, buyers fees and reimbursable advances from the proceeds of auctioned salvage vehicles.

As of October 31, 2006, we had working capital of approximately $353.3 million, including cash, cash equivalents and short-term investments of approximately $313.7 million. During the course of the year, we invest substantially all of our cash balances in AAA-rated auction rate securities and typically convert a portion of these securities to cash and cash equivalents prior to the end of each quarter. Auction rate securities are principally variable rate securities tied to short-term interest rates with maturities on the face of the securities in excess of 90 days. Auction rate securities have interest rate resets through a modified Dutch auction, at predetermined short-term intervals, usually every 7, 28 or 35 days. They trade at par and are callable at par on any interest payment date at the option of the issuer. Interest paid during a given period is based upon the interest rate determined during the prior auction. Although these instruments are issued and rated as long-term securities, they are priced and traded as short-term securities because of the liquidity provided through the interest rate reset.

We believe that our currently available cash, cash equivalents and short-term investments and cash generated from operations will be sufficient to satisfy our operating and working capital requirements for at least the next 12 months. However, if we experience significant growth in the future, we may be required to raise additional cash through the issuance of new debt or additional equity.

Operating Activities

Net cash provided by operating activities increased by approximately $23.6 million to $53.9 million during the three months ended October 31, 2006 when compared to the three months ended October 31, 2005, due to the timing of routine changes in working capital items. The increase in net income is primarily a result of increased revenue due to growth in vehicle sales volume and higher fees resulting from increased auction proceeds per vehicle.

Investing Activities

During the three months ended October 31, 2006, we purchased approximately $213.8 million in short-term investments. These purchases were partially offset by the sale of $175.5 million of short-term investments. We typically invest our cash in auction rate notes with ratings of AAA.

Capital expenditures related to continuing operations (excluding those associated with fixed assets attributable to acquisitions) were approximately $21.1 million and $23.5 million for three months ended October 31, 2006 and 2005, respectively. Our capital expenditures are related primarily to opening and improving facilities and acquiring yard equipment. We continue to expand and invest in new and existing facilities in order to handle increased volume and standardize the appearance of existing locations.

During the three months ended October 31, 2006, we did not acquire any facilities. During the three months ended October 31, 2005, we used cash for the acquisition of facilities in or near Greenwood, Nebraska and Grand Island, Nebraska, which had an aggregate cash cost of approximately $3.3 million.

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During the three months ended October 31, 2005 the Company committed to invest $9.0 million for a 50% equity interest in Lanelogic, of which $3.0 million was contributed during the three months ended October 31, 2005 and $6.0 million was contributed during the three months ended January 31, 2006.

Financing Activities

For the three months ended October 31, 2006 and 2005, we generated approximately $1.6 million and $1.7 million, respectively, through the exercise of stock options.

In February 2003, our Board of Directors authorized us to repurchase up to 9.0 million shares of our common stock. The repurchases may be effected through solicited or unsolicited transactions in the open market or in privately negotiated transactions. No time limit has been placed on the duration of the share repurchase program. The repurchases will be made at such times and in such amounts as we deem appropriate and may be discontinued at any time. For the year ended July 31, 2006, we repurchased 366,000 shares at a weighted average price of $24.24. For the year ended July 31, 2005, we did not repurchase any shares. We did not repurchase any shares during the three months ended October 31, 2006. The total number of shares repurchased under the program as of October 31, 2006 is approximately 4.0 million, leaving approximately 5.0 million available under the repurchase program.

Lease, Purchase and Other Contractual Obligations

The following table summarizes our significant contractual obligations and commercial commitments as of October 31, 2006 (in thousands):

	Payments due by period				
Contractual Obligations (1)	**Total**	**Less than 1 year**	**1-3 years**	**3-5 years**	**More than 5 years**
Operating leases	$ 117,771	$ 22,099	$ 34,765	$ 26,294	$ 34,613

	Amount of commitment expiration per period				
Commercial Commitments (2)	**Total**	**Less than 1 year**	**1-3 years**	**3-5 years**	**More than 5 years**
Letters of credit	$ 10,000	$ 10,000	$	$	$

(1) Contractual obligations consist of future non-cancelable minimum lease payments under operating leases entered into in the ordinary course of business.

(2) Commercial commitments include primarily letters of credit provided for insurance programs and certain business transactions.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our principal exposures to financial market risk are interest rate and foreign currency risk. Our exposure to market risk for changes in interest rates relates primarily to our investment portfolio of marketable securities. As of October 31, 2006, our cash, cash equivalents and short-term investments consisted primarily of funds invested in money market accounts, which bear interest at a variable rate and AAA rated auction rate securities, which also bear interest at a variable rate. Due to the average maturity and nature of the Company s investment portfolio, we believe a sudden change in interest rates would not have a material effect on the value of our investment portfolio. As the interest rates on a material portion of our cash, cash equivalents and short-term investments are variable, a change in interest rates earned on our investment portfolio would impact interest income along with cash flows, but would not materially impact the fair market value of the related underlying instruments.

Our exposure to foreign currency risks relates to our operations in Canada, which have not been significant. We do not hedge our exposure to the Canadian dollar. We do not use derivative financial instruments for speculative or trading purposes.

ITEM 4. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures

We conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, or Disclosure Controls, as of the end of the period covered by this quarterly report on Form 10-Q. This evaluation, or Controls Evaluation was performed under the supervision and with the participation of management, including our Chairman of the Board, Chief Executive Officer and Director (our CEO) and our Senior Vice President and Chief Financial Officer (our CFO). Disclosure Controls are controls and procedures designed to provide reasonable assurance that information required to be disclosed in our reports filed under the Securities Exchange Act of 1934, as amended (the Exchange Act), such as this quarterly report, is recorded, processed, summarized and reported within the time periods specified in the U.S. Securities and Exchange Commission s rules and forms. Disclosure Controls include, without limitation, controls and procedures designed to provide reasonable assurance that information required to be disclosed in our reports filed under the Exchange Act is accumulated and communicated to our management, including our CEO and CFO, or persons performing similar functions, as appropriate, to allow timely decisions regarding required disclosure. Our Disclosure Controls include some, but not all, components of our internal control over financial reporting.

Based upon the Controls Evaluation, our CEO and CFO have concluded that as of the end of the period covered by this quarterly report on Form 10-Q, our Disclosure Controls were effective to provide reasonable assurance that information required to be disclosed in our Exchange Act reports is accumulated and communicated to management, including the CEO and CFO, to allow timely decisions regarding required disclosure, and that such information is recorded, processed, summarized and reported within the time periods specified by the Securities and Exchange Commission.

(b) Changes in Internal Controls

There were no changes in our internal control over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are involved in litigation and damage claims arising in the ordinary course of business, such as actions related to injuries, property damage, and handling or disposal of vehicles. This litigation includes the following matters:

Ciano Dessources filed a lawsuit on May 21, 2003, in the Commonwealth of Massachusetts, Superior Court Department against Copart of Connecticut, Inc., and Copart, Inc., which purported to be a class action on behalf of persons whose vehicles were disposed of by us as abandoned vehicles and which the named plaintiff contends were disposed of without complying with state laws. Relief sought includes class certification, declaratory, remedial and/or injunctive relief, including the ordering of a compliance program that will essentially protect consumers, as well as damages, fees, and costs. Our motion for summary judgment was granted on December 8, 2004, dismissing the class claim element of the lawsuit. On August 9, 2006, plaintiff s motion for summary judgment was denied. A trial date has been set for March 5, 2007. We believe the claim is without merit, and are defending the lawsuit vigorously.

On September 16, 2005, Richard M. Gray filed suit against Copart and A. Safrin, in the State Court for the County of Chatham, State of Georgia, alleging a class action for unreasonable amounts claimed for storage liens by us, and related claims. Relief sought includes class certification, damages, fees, costs and expenses. Our motion for summary judgment was heard on December 4, 2006 and no decision has yet been made. We believe the claim is without merit, and are defending the lawsuit vigorously.

On July 28, 2006, Foreign Car Sales and Service LLC filed suit against Copart in the United States District Court for the Middle District of Louisiana alleging antitrust violations and unfair trade practices. Relief sought includes class certification, damages, fees, costs and expenses. Plaintiff is in pro per and is demanding a total award of the now current value of 51% of our issued stock. We believe the claim is without merit, and are defending the lawsuit vigorously.

On August 7, 2006, Kimberly and Jason Green filed suit against Copart in the Superior Court of the State of California, County of Sacramento, making allegations pursuant to a California consumer protection statute similar to a class action for unreasonable amounts claimed for storage liens by us, and related claims. Relief sought includes class certification, damages, fees, costs and expenses. We filed an answer on September 1, 2006 denying the claim. We believe the claim is without merit, and are defending the lawsuit vigorously.

We provide for costs relating to these matters when a loss is probable and the amount can be reasonably estimated. The effect of the outcome of these matters on our future results of operations cannot be predicted because any such effect depends on future results of operations, and the amount and timing of the resolution of such matters. We believe that any ultimate liability will not have a material effect on its financial position, results of operations or cash flows. However, the amount of the liabilities associated with these claims, if any, cannot be determined with certainty.

ITEM 1A. RISK FACTORS

Set forth below and elsewhere in this report and in other documents we file with the SEC are descriptions of the risks and uncertainties that could cause our actual results to differ materially from the results contemplated by the forward-looking statements contained in this report.

We depend on a limited number of major suppliers of salvage vehicles. The loss of one or more of these major suppliers could adversely affect our results of operations and financial condition, and an inability to increase our sources of vehicle supply could adversely affect our growth rates.

Historically, a limited number of vehicle suppliers have accounted for a substantial portion of our revenues. In the first quarter of fiscal 2007, vehicles supplied by our largest supplier accounted for approximately 11% of our revenues. Supplier arrangements are either written or oral agreements typically subject to cancellation by either party upon 30 to 90 days notice. Vehicle suppliers have terminated agreements with us in the past in particular markets, which has affected the pricing for sales services in those markets. There can be no assurance that our existing agreements will not be cancelled. Furthermore, there can be no assurance that we will be able to enter into future agreements with vehicle suppliers or that we will be able to retain our existing supply of salvage vehicles. A reduction in vehicles from a significant vehicle supplier or any material changes in the terms of an arrangement with a substantial vehicle supplier could have a material adverse effect on our results of operations and financial condition. In addition, a failure to increase our sources of vehicle supply could adversely affect our earnings and revenue growth rates.

Our strategic shift from live salvage sales to an entirely Internet-based sales model presents new risks, including substantial technology risks.

In fiscal 2004, we converted all our salvage sales from a live auction process to an entirely Internet-based auction-style model based on technology developed internally by us. The conversion represents a significant change in the way we conduct business and presents numerous risks, including our increased reliance on the availability and reliability of our network systems. In particular, we believe the conversion presents the following risks, among others:

- Our operating results in a particular period could be adversely affected in the event our networks are not operable for an extended period of time for any reason, as a result of Internet viruses, or as a result of any other technological circumstance that makes us unable to conduct our virtual sales.

- Our business is increasingly reliant on internally developed technology, and we have limited historic experience developing technologies or systems for large-scale implementation and use.

- Our general and administrative expenses have tended to increase as a percentage of revenue as our information technology payroll has increased.

- The change in our business model may make it more difficult for management, investment analysts, and investors to model or predict our future operating results until sufficient historic data is available to evaluate the effect of the VB2 implementation over a longer period of time and in different economic environments.

- Our increasing reliance on proprietary technology subjects us to intellectual property risks, including the risk of third party infringement claims or the risk that we cannot establish or protect intellectual property rights in our technologies. We have filed patent applications for VB2 in the United States, Netherlands, and Europe, but we cannot provide any assurances that patents will actually issue or that, if issued, the patent could not later be found to be unenforceable or invalid.

Our operating results were adversely affected by abnormal expenses associated with Hurricanes Katrina and Rita during the year ended July 31, 2006, and our operating margins in future periods could be adversely affected by the hurricanes.

During the year ended July 31, 2006, we recognized substantial additional costs associated with Hurricanes Katrina and Rita. These additional costs, characterized as abnormal under SFAS 151, were recognized during the year ended July 31, 2006, and include the additional subhauling, payroll, equipment and facilities expenses directly related to the operating conditions created by the hurricanes. We expect these costs to continue in future periods. These abnormal costs do not include the normal expenses associated with the increased unit volume created by the hurricanes, which are deferred until the sale of the unit and are reflected in vehicle pooling costs on the balance sheet. As of October 31, 2006, approximately 10.6% of the incremental salvage vehicles received as a result of the hurricanes remained unsold and in inventory. The Company expects that the majority of these vehicles will be disposed of primarily in the second quarter of fiscal 2007. The Company s expectation that we will sell the balance of the unsold hurricane-related vehicles primarily within the second quarter of fiscal 2007 is based on management s current expectations, which assumes, among other things, that the Gulf Coast region will not experience any additional adverse weather events. The normal costs that have been capitalized will be recognized as yard expense as the vehicles are sold.

Our results of operations may not continue to benefit from the implementation of VB2 to the extent we have experienced in recent periods.

We believe that the implementation of our proprietary VB2 sales technologies across our salvage operations has had a favorable impact on our results of operations by increasing the size and geographic scope of our buyer base and increasing the average selling price for vehicles sold through our sales. VB2 was implemented across all our salvage yards beginning in the third quarter of fiscal 2004. We do not believe, however, that we will continue to experience improvements in our results of operations at the same relative rates we have experienced in the last few years.

Failure to have sufficient capacity to accept additional cars at one or more of our salvage yards could adversely affect our relationships with insurance companies or other suppliers of salvage vehicles.

Capacity at our salvage yards varies from period to period and from region to region. For example, following adverse weather conditions in a particular area, our yards in that area may fill and limit our ability to accept additional salvage vehicles while we process existing inventories. For example, as discussed above, Hurricanes Katrina and Rita had an adverse effect on our operating results, in part because of yard capacity constraints in the Gulf Coast area. We regularly evaluate our capacity in all our markets and, where appropriate, seek to increase capacity through the acquisition of additional land and yards. We may not be able to reach agreements to purchase independent salvage yards in markets where we have limited excess capacity, and zoning restrictions or difficulties obtaining use permits may limit our ability to expand our capacity through acquisitions of new land. Failure to have sufficient capacity at one or more of our yards could adversely affect our relationships with insurance companies or other suppliers of salvage vehicles, which could have an adverse effect on our operating results.

Factors such as mild weather conditions in the United States can have an adverse effect on our revenues and operating results as well as our revenue and earnings growth rates.

Mild weather conditions in the United States tend to result in a decrease in the available supply of salvage vehicles because traffic accidents decrease and fewer automobiles are damaged. Accordingly, mild weather can have an adverse effect on our salvage vehicle inventories, which would be expected to have an adverse effect on our revenue and operating results and related growth rates. Conversely, our inventories will tend to increase in poor weather such as a harsh winter or as a result of adverse weather-related conditions such as flooding. During periods of mild weather conditions, our ability to increase our revenues and improve our operating results and related growth will be increasingly dependent on our ability to obtain additional vehicle suppliers and to compete more effectively in the market, each of which is subject to the other risks and uncertainties described in these sections.

High fuel prices in the United States and Canada may have an adverse effect on our revenues and operating results as well as our earnings growth rates.

Significant increases in the cost of fuel could lead to a reduction in miles driven per car and a reduction in accident rates. A material reduction in accident rates could have a material impact on revenue growth. In addition, under our PIP contracts the cost of towing the vehicle to one of our facilities is included in the PIP fee. We may incur increased fees which we will not be able to pass on to the insurance companies. A material increase in tow rates could have a material impact on our operating results.

The salvage vehicle sales industry is highly competitive and we may not be able to compete successfully.

We face significant competition for the supply of salvage vehicles and for the buyers of those vehicles. We believe our principal competitors include other vehicle sales and auction companies with whom we compete directly in obtaining vehicles from insurance companies and other suppliers, and large vehicle dismantlers, who may buy salvage vehicles directly from insurance companies, bypassing the salvage sales process. Many of the insurance companies have established relationships with competitive sales and auction companies and large dismantlers. Certain of our competitors may have greater financial resources than us. Due to the limited number of vehicle suppliers, the absence of long-term contractual commitments between us and our suppliers and the increasingly competitive market environment, there can be no assurance that our competitors will not gain market share at our expense.

We may also encounter significant competition for local, regional and national supply agreements with vehicle suppliers. There can be no assurance that the existence of other local, regional or national contracts entered into by our competitors will not have a material adverse effect on our business or our expansion plans. Furthermore, we are likely to face competition from major competitors in the acquisition of salvage vehicle sales facilities, which could significantly increase the cost of such acquisitions and thereby materially impede our expansion objectives or have a material adverse effect on our results of operations. These potential new competitors may include consolidators of automobile dismantling businesses, organized salvage vehicle buying groups, automobile manufacturers, automobile auctioneers and software companies. While most vehicle suppliers have abandoned or reduced efforts to sell salvage vehicles directly without the use of service providers such as us, there can be no assurance that this trend will continue, which could adversely affect our market share, results of operations and financial condition. Additionally, existing or new competitors may be significantly larger and have greater financial and marketing resources than us; therefore, there can be no assurance that we will be able to compete successfully in the future.

Because the growth of our business has been due in large part to acquisitions and development of new salvage vehicle sales facilities, the rate of growth of our business and revenues may decline if we are not able to successfully complete acquisitions and development of new facilities.

We seek to increase our sales and profitability through the acquisition of other salvage vehicle sales facilities and the development of new salvage vehicle storage facilities. There can be no assurance that we will be able to:

- continue to acquire additional facilities on favorable terms;
- expand existing facilities in no-growth regulatory environments;
- increase revenues and profitability at acquired and new facilities;
- maintain the historical revenue and earnings growth rates we have been able to obtain through facility openings and strategic acquisitions; or

- create new salvage vehicle storage facilities that meet our current revenue and profitability requirements.

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As we continue to expand our operations, our failure to manage growth could harm our business and adversely affect our results of operations and financial condition.

Our ability to manage growth is not only dependent on our ability to successfully integrate new facilities, but also on our ability to:

- hire, train and manage additional qualified personnel;
- establish new relationships or expand existing relationships with vehicle suppliers;
- identify and acquire or lease suitable premises on competitive terms;
- secure adequate capital; and
- maintain the supply of vehicles from vehicle suppliers.

Our inability to control or manage these growth factors effectively could have a material adverse effect on our financial position, results of operations, or cash flows.

Our annual and quarterly performance may fluctuate, causing the price of our stock to decline.

Our revenues and operating results have fluctuated in the past and can be expected to continue to fluctuate in the future on a quarterly and annual basis as a result of a number of factors, many of which are beyond our control. Factors that may affect our operating results include, but are not limited to, the following:

- fluctuations in the market value of salvage and used vehicles;
- the availability of salvage vehicles;
- variations in vehicle accident rates;
- buyer participation in the Internet bidding process;
- delays or changes in state title processing;
- changes in state or federal laws or regulations affecting salvage vehicles;
- changes in state laws affecting who may purchase salvage vehicles;
- our ability to integrate and manage our acquisitions successfully;
- the timing and size of our new facility openings;
- the announcement of new vehicle supply agreements by us or our competitors;
- severity of weather and seasonality of weather patterns;
- the amount and timing of operating costs and capital expenditures relating to the maintenance and expansion of our business, operations and infrastructure;
- the availability and cost of general business insurance;

- labor costs and collective bargaining;
- availability of subhaulers at competitive rates;
- acceptance of buyers and sellers of our Internet-based model deploying VB2, a proprietary Internet auction-style sales technology;
- changes in the current levels of out of state and foreign demand for salvage vehicles;
- the introduction of a similar Internet product by a competitor; and
- the ability to obtain necessary permits to operate salvage storage facilities.

Due to the foregoing factors, our operating results in one or more future periods can be expected to fluctuate. As a result, we believe that period-to-period comparisons of our results of operations are not necessarily meaningful and should not be relied upon as any indication of future performance. In the event such fluctuations result in our financial performance being below the expectations of public market analysts and investors, the price of our common stock could decline substantially.

Our strategic shift to an Internet-based sales model has increased the relative importance of intellectual property assets to our business, and any inability to protect those rights could have a material adverse effect on our business, financial condition, or results of operations.

Implementation of VB2 across our salvage operations has increased the relative importance of intellectual property rights to our business. Our intellectual property rights include pending patent applications for VB2 as well as trademarks, trade secrets, copyrights and other intellectual property rights. We are in the process of prosecuting an initial patent application relating to VB2 and cannot predict whether a patent will actually issue from that application. Even if a patent is issued, the scope of the protection gained may be insufficient or any issued patent could subsequently be deemed invalid or unenforceable. In addition, we are increasingly entering into agreements

with third parties regarding the license or other use of our intellectual property in foreign jurisdictions. Effective intellectual property protection may not be available in every country in which our products and services are distributed, deployed, or made available. We seek to maintain certain intellectual property rights as trade secrets. The secrecy could be compromised by third parties, or intentionally or accidentally by our employees, which would cause us to lose the competitive advantage resulting from those trade secrets. Any significant impairment of our intellectual property rights, or any inability to protect our intellectual property rights, could have a material adverse effect on our financial position, results of operations, or cash flows.

We have in the past been and may in the future be subject to intellectual property rights claims, which are costly to defend, could require us to pay damages, and could limit our ability to use certain technologies in the future.

Litigation based on allegations of infringement or other violations of intellectual property rights are common among companies who rely heavily on intellectual property rights. Our reliance on intellectual property rights has increased significantly in recent years as we have implemented our VB2 auction-style sales technologies across our business and abandoned live auctions. As we face increasing competition, the possibility of intellectual property rights claims against us grows. Litigation and any other intellectual property claims, whether with or without merit, can be time-consuming, expensive to litigate and settle, and can divert management resources and attention from our core business. An adverse determination in current or future litigation could prevent us from offering our products and services in the manner currently conducted. We may also have to pay damages or seek a license for the technology, which may not be available on reasonable terms and which may significantly increase our operating expenses, if it is available for us to license at all. We could also be required to develop alternative non-infringing technology, which could require significant effort and expense.

New accounting pronouncements or new interpretations of existing standards could require us to make adjustments in our accounting policies that could adversely affect our financial statements.

The Financial Accounting Standards Board, the Securities and Exchange Commission, or other accounting organizations or governmental entities issue new pronouncements or new interpretations of existing accounting standards that may require us to change our accounting policies and procedures. To date, we do not believe any new pronouncements or interpretations have had an adverse effect on our financial condition or results of operations, but future pronouncements or interpretations could require us to change our policies or procedures. Moreover, we continually review our critical accounting policies in light of the accounting literature and changes in our operations.

Government regulation of the salvage vehicle sales and auction industry may impair our operations, increase our costs of doing business and create potential liability.

Participants in the salvage vehicle sales and auction industry are subject to, and may be required to expend funds to ensure compliance with a variety of U.S. or Canadian, federal, state, provincial and local governmental, regulatory and administrative rules, regulations, land use ordinances, licensure requirements and procedures, including those governing vehicle registration, the environment, zoning and land use. Failure to comply with present or future regulations or changes in interpretations of existing regulations may result in impairment of our operations and the imposition of penalties and other liabilities. At various times, we may be involved in disputes with local governmental officials regarding the development and/or operation of our business facilities. We believe that we are in compliance in all material respects with applicable regulatory requirements. We may be subject to similar types of regulations by federal, provincial, state, and local governmental agencies in new markets. In addition, new regulatory requirements or changes in existing requirements may delay or increase the cost of opening new facilities, may limit our base of salvage vehicle buyers and may decrease demand for our vehicles.

The operation of our storage facilities poses certain environmental risks, which could adversely affect our financial position, results of operations or cash flows.

Our operations are subject to federal, state, provincial and local laws and regulations regarding the protection of the environment. In the salvage vehicle sales industry, large numbers of wrecked vehicles are stored at storage facilities and, during that time, spills of fuel, motor oil and other fluids may occur, resulting in soil, surface water or groundwater contamination. In addition, certain of our facilities generate and/or store petroleum products and other hazardous materials, including waste solvents and used oil. We could incur substantial expenditures for preventative, investigative or remedial action and could be exposed to liability arising from our operations, contamination by previous users of certain of our acquired facilities, or the disposal of our waste at off-site locations. Environmental laws and regulations could become more stringent over time and there can be no assurance that we or our operations will not be subject to significant costs in the future. Although we have obtained indemnification for pre-existing environmental liabilities from many of the persons and entities from whom we have acquired facilities, there can be no assurance that such indemnifications will be adequate. Any such expenditures or liabilities could have a material adverse effect on our results of operations and financial condition.

If we experience problems with our providers of fleet operations, our business could be harmed.

We rely upon independent subhaulers to pick up and deliver vehicles to and from our storage facilities. Our failure to pick up and deliver vehicles in a timely and accurate manner could harm our reputation and brand, which could have a material adverse effect on our business. Further, an increase in fuel cost may lead to increased prices charged by our independent subhaulers, which may significantly increase our cost. These costs may not be passed on to our sellers or buyers.

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We are partially self-insured for certain losses.

We are partially self-insured for certain losses related to medical insurance, general liability, workers compensation and auto liability. Our liability represents an estimate of the ultimate cost of claims incurred as of the balance sheet date. The estimated liability is not discounted and is established based upon analysis of historical data and actuarial estimates. While we believe these estimates are reasonable based on the information currently available, if actual trends, including the severity of claims and medical cost inflation, differ from our estimates, our results of operations could be impacted. Further, we rely on independent actuaries to assist us in establishing the proper amount of reserves for anticipated payouts associated with these self-insured exposures.

Our executive officers, directors and their affiliates hold a large percentage of our stock and their interests may differ from other shareholders.

Our executive officers, directors and their affiliates beneficially own, in the aggregate, approximately 21% of our common stock as of October 31, 2006. If they were to act together, these shareholders would have significant influence over most matters requiring approval by shareholders, including the election of directors, any amendments to our articles of incorporation and certain significant corporate transactions, including potential merger or acquisition transactions. In addition, without the consent of these shareholders, we could be delayed or prevented from entering into transactions that could be beneficial to us or our other investors. These shareholders may take these actions even if they are opposed by our other investors.

We have a shareholder rights plan, or poison pill, which could affect the price of our common stock and make it more difficult for a potential acquirer to purchase a large portion of our securities, to initiate a tender offer or a proxy contest, or to acquire us.

In March 2003, our board of directors adopted a shareholder rights plan, commonly known as a poison pill. The poison pill may discourage, delay, or prevent a third party from acquiring a large portion of our securities, initiating a tender offer or proxy contest, or acquiring us through an acquisition, merger, or similar transaction. Such an acquirer could be prevented from consummating one of these transactions even if our shareholders might receive a premium for their shares over then-current market prices.

If we lose key management or are unable to attract and retain the talent required for our business, we may not be able to successfully manage our business or achieve our objectives.

Our future success depends in large part upon the leadership and performance of our executive management team, all of whom are employed on an at-will basis and none of whom are subject to any agreements not to compete. If we lose the service of one or more of our executive officers or key employees, in particular Willis J. Johnson, our Chief Executive Officer, and A. Jayson Adair, our President, or if one or more of them decides to join a competitor or otherwise compete directly or indirectly with us, we may not be able to successfully manage our business or achieve our business objectives.

Compliance with new rules and regulations concerning corporate governance may be costly and time consuming.

The Sarbanes-Oxley Act of 2002, or Sarbanes-Oxley, requires, among other things, that companies adopt new corporate governance measures, imposes comprehensive reporting and disclosure requirements, sets stricter independence and financial expertise standards for board and audit committee members and imposes increased civil and criminal penalties for companies, their chief executive officers and chief financial officers for securities law violations. In addition, the Nasdaq Global Select Market, on which our common stock is traded, has adopted additional comprehensive rules and regulations relating to corporate governance. These laws, rules and regulations will increase the scope, complexity and cost of our corporate governance, reporting and disclosure practices, which could harm our results of operations and divert management s attention from business operations. These new rules and regulations may also make it more difficult and more expensive for us to obtain director and officer liability insurance and make it more difficult for us to attract and retain qualified members of our board of directors, particularly to serve on our audit committee.

ITEM 6. EXHIBITS

(a) Exhibits

31.1	Certification of Willis J. Johnson, Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of William E. Franklin, Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of Willis J. Johnson, Chief Executive Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of William E. Franklin, Chief Financial Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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SIGNATURES

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

COPART, INC.

/s/ William E. Franklin
William E. Franklin, Senior Vice President and Chief Financial Officer (duly authorized officer and principal financial and accounting officer)

Date: December 8, 2006

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