MONEYGRAM INTERNATIONAL INC
Form 10-Q
November 10, 2008

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(mark one)

þ **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the Quarterly Period Ended September 30, 2008**

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: 001-31950

MONEYGRAM INTERNATIONAL, INC.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	16-1690064 (I.R.S. Employer Identification No.)
1550 Utica Avenue South, Suite 100, Minneapolis, Minnesota (Address of principal executive offices)	55416 (Zip Code)

(952) 591-3000
(Registrant s telephone number, including area code)

Not applicable
(Former name, former address and former fiscal year, if changed since last report)

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 þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer þ	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company 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 þ

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

As of November 3, 2008, 82,555,904 shares of Common Stock, $0.01 par value, were outstanding.

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PART I. FINANCIAL INFORMATION

Item 1, FINANCIAL STATEMENTS

MONEYGRAM INTERNATIONAL, INC.
CONSOLIDATED BALANCE SHEETS
UNAUDITED

(Amounts in thousands, except share data)	**September 30 2008**	**December 31 2007**
ASSETS		
Cash and cash equivalents	$	$
Cash and cash equivalents (substantially restricted)	4,561,905	1,552,949
Receivables, net (substantially restricted)	1,397,179	1,408,220
Trading investments (substantially restricted)	30,285	62,105
Available for sale investments (substantially restricted)	480,944	4,187,384
Property and equipment	157,484	171,008
Derivative financial instruments		1,647
Intangible assets	15,051	17,605
Goodwill	443,758	438,839
Other assets	174,443	95,254
Total assets	$7,261,049	$7,935,011
LIABILITIES		
Payment service obligations	$6,101,759	$7,762,470
Debt	978,869	345,000
Derivative financial instruments		30,370
Pension and other postretirement benefits	89,514	85,451
Deferred tax liabilities	19,893	11,459
Accounts payable and other liabilities	200,393	188,778
Total liabilities	7,390,428	8,423,528
COMMITMENTS AND CONTINGENCIES (NOTE 13)		
MEZZANINE EQUITY		
Participating Convertible Preferred Stock-Series B, $0.01 par value, 800,000 shares authorized, 495,000 shares issued and outstanding	439,655	
Participating Convertible Preferred Stock-Series B-1, $0.01 par value, 500,000 shares authorized, 272,500 shares issued and outstanding	274,230	
Total mezzanine equity	713,885	
STOCKHOLDERS DEFICIT		
Preferred shares undesignated, $0.01 par value, 5,000,000 authorized, none issued		
Preferred shares junior participating, $0.01 par value, 2,000,000 authorized, none issued		

Common shares, $0.01 par value, 250,000,000 shares authorized, 88,556,077 shares issued	886	886
Additional paid-in capital	91,211	73,077
Retained loss	(772,115)	(387,479)
Unearned employee benefits	(693)	(3,280)
Accumulated other comprehensive loss	(9,992)	(21,715)
Treasury stock: 6,000,173 and 5,910,458 shares at September 30, 2008 and December 31, 2007, respectively	(152,561)	(150,006)
Total stockholders deficit	(843,264)	(488,517)
Total liabilities, mezzanine equity and stockholders deficit	$7,261,049	$7,935,011

See Notes to Consolidated Financial Statements

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MONEYGRAM INTERNATIONAL, INC.
CONSOLIDATED STATEMENTS OF (LOSS) INCOME
UNAUDITED

	Three Months Ended September 30		Nine Months Ended September 30	
(Amounts in thousands, except per share data)	**2008**	**2007**	**2008**	**2007**
REVENUE				
Fee and other revenue	$286,021	$242,743	$ 830,699	$688,409
Investment revenue	32,231	102,000	128,294	299,161
Net securities losses	(13,253)	(3,162)	(350,844)	(2,679)
Total revenue	304,999	341,581	608,149	984,891
Fee commissions expense	131,397	105,453	377,727	295,744
Investment commissions expense	9,968	64,899	101,472	192,467
Total commissions expense	141,365	170,352	479,199	488,211
Net revenue	163,634	171,229	128,950	496,680
EXPENSES				
Compensation and benefits	53,541	49,572	173,976	149,966
Transaction and operations support	48,530	44,277	151,894	128,129
Depreciation and amortization	13,891	13,944	42,397	37,835
Occupancy, equipment and supplies	11,069	11,975	34,682	33,377
Interest expense	27,834	2,202	66,631	6,143
Valuation loss on embedded derivatives	47,233		16,030	
Debt extinguishment loss			1,499	
Total expenses	202,098	121,970	487,109	355,450
(Loss) income before income taxes	(38,464)	49,259	(358,159)	141,230
Income tax expense	88	14,967	26,087	44,740
NET (LOSS) INCOME	$ (38,552)	$ 34,292	$(384,246)	$ 96,490
Basic (loss) earnings per common share	$ (0.80)	$ 0.42	$ (5.34)	$ 1.16
Diluted (loss) earnings per common share	$ (0.80)	$ 0.41	$ (5.34)	$ 1.15
Net (loss) income	$ (38,552)	$ 34,292	$(384,246)	$ 96,490
Preferred stock dividends	(24,995)		(50,810)	
Accretion recognized on preferred stock	(2,533)		(5,192)	
(Loss) earnings allocated to preferred stockholders				
(Loss) income available to common stockholders	$ (66,080)	$ 34,292	$(440,248)	$ 96,490

Average outstanding common shares	82,464	82,488	82,452	82,956
Additional dilutive shares related to stock-based compensation		963		1,183
Additional dilutive shares related to preferred stock				
Average outstanding and potentially dilutive common shares	82,464	83,451	82,452	84,139

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MONEYGRAM INTERNATIONAL, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS) INCOME
UNAUDITED

(Amounts in thousands)	Three Months Ended September 30 2008	Three Months Ended September 30 2007	Nine Months Ended September 30 2008	Nine Months Ended September 30 2007
NET (LOSS) INCOME	$(38,552)	$ 34,292	$(384,246)	$ 96,490
OTHER COMPREHENSIVE INCOME (LOSS)				
Net unrealized gains (losses) on available-for-sale securities:				
Net holding gains (losses) arising during the period, net of tax expense (benefit) of $5,401 and ($88,785) for the three months ended September 30, 2008 and 2007, respectively, and $10,807 and ($126,075) for the nine months ended September 30, 2008 and 2007, respectively	8,813	(144,857)	17,633	(205,699)
Reclassification adjustment for net realized (gains) losses included in net income, net of tax (expense) benefit of ($1,076) and $1,202 for the three months ended September 30, 2008 and 2007, respectively, and ($16,282) and $1,018 for the nine months ended September 30, 2008 and 2007, respectively	(1,756)	1,961	(26,565)	1,661
	7,057	(142,896)	(8,932)	(204,038)
Net unrealized gains (losses) on derivative financial instruments:				
Net holding gains (losses) arising during the period, net of tax expense of $1,148 and ($9,716) for the three months ended September 30, 2008 and 2007, respectively and $1,196 and ($4,836) for the nine months ended September 30, 2008 and 2007, respectively	1,872	(15,854)	1,951	(7,891)
Reclassifications adjustment for net unrealized (gains) losses included in net income, net of tax (expense) benefit of ($976) for the three months ended September 30, 2007, and $11,006 and ($4,306) for the nine months ended September 30, 2008 and 2007, respectively		(1,592)	17,957	(7,025)

	1,872	(17,446)	19,908	(14,916)
Prior service (credit) costs for pension and postretirement benefit plans: Reclassification of prior service (credit) costs recorded to net income, net of tax (expense) benefit of ($23) and $18 for the three months ended September 30, 2008 and 2007, respectively, and $181 and $54 for the nine months ended September 30, 2008 and 2007, respectively	(37)	29	296	88
Net actuarial (gain) loss for pension and postretirement benefit plans: Reclassification of net actuarial (gain) loss recorded to net income, net of tax (expense) benefit of ($104) and $417 for the three months ended September 30, 2008 and 2007, respectively, and $395 and $1,251 for the nine months ended September 30, 2008 and 2007, respectively	(169)	662	645	1,986
Unrealized foreign currency translation (losses) gains, net of tax (benefit) expense of ($491) and $815 for the three months ended September 30, 2008 and 2007, respectively, and $780 and $1,368 for the nine months ended September 30, 2008 and 2007, respectively	(800)	1,330	1,273	2,233
Other comprehensive income (loss)	7,923	(158,321)	13,190	(214,647)
COMPREHENSIVE LOSS	$(30,629)	$(124,029)	$(371,056)	$(118,157)

See Notes to Consolidated Financial Statements

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MONEYGRAM INTERNATIONAL, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
UNAUDITED

	Three Months Ended September 30		Nine Months Ended September 30	
(Amounts in thousands)	**2008**	**2007**	**2008**	**2007**
CASH FLOWS FROM OPERATING ACTIVITIES:				
Net (loss) income	$ (38,552)	$ 34,292	$ (384,246)	$ 96,490
Adjustments to reconcile net (loss) income to net cash used in operating activities:				
Investment impairment charges	8,327	4,629	62,725	6,124
Net loss (gain) on sale of investments		(1,467)	256,298	(3,445)
Unrealized losses on trading investments	4,925		31,820	
Non-cash valuation loss on embedded derivative	47,233		16,030	
Net amortization of investment premiums and (discounts)	68	(3,895)	558	(12,989)
Depreciation and amortization	13,891	13,944	42,397	37,835
Signing bonus amortization	10,712	6,716	27,809	19,286
Amortization of debt discount and deferred financing costs	2,444	40	5,057	120
Debt extinguishment loss			1,499	
Provision for uncollectible receivables	1,458	2,828	6,966	6,780
Non-cash compensation and pension expense	2,550		6,600	
Changes in foreign currency translation adjustments	(800)	1,330	1,273	2,233
Other non-cash items, net	2,426	(2,921)	2,917	(8,192)
Change in other assets	(4,986)	(8,039)	(58,422)	(5,288)
Change in accounts payable and other liabilities	(4,440)	11,936	23,933	21,917
Total adjustments	83,808	25,101	427,460	64,381
Change in cash and cash equivalents (substantially restricted)	(75,840)	(161,391)	(3,008,925)	(166,296)
Change in trading investments, net (substantially restricted)		58,900		83,200
Change in receivables, net (substantially restricted)	558,617	55,140	1,889	34,439
Change in payment service obligations	(534,813)	(304,142)	(1,660,726)	(302,396)
Net cash used in continuing operating activities	(6,780)	(292,100)	(4,624,548)	(190,182)
CASH FLOWS FROM INVESTING ACTIVITIES:				
		12,112	2,896,011	321,687

Proceeds from sales of investments classified as available-for-sale				
Proceeds from maturities of investments classified as available-for-sale	19,507	148,710	465,603	536,569
Purchases of investments classified as available-for-sale		(29,391)		(758,898)
Purchases of property and equipment	(9,232)	(23,431)	(26,669)	(53,442)
Cash paid for acquisitions, net of cash acquired	(2,870)		(2,870)	(1,116)
Net cash provided by investing activities	7,405	108,000	3,332,075	44,800
CASH FLOWS FROM FINANCING ACTIVITIES:				
Proceeds from issuance of debt			733,750	
Transaction costs for issuance or amendment of debt			(47,805)	
Payment on debt	(625)		(1,250)	
Net change in credit facilities		197,000		197,000
Payment on revolving facility			(100,000)	
Proceeds from issuance of preferred stock			760,000	
Transaction costs for issuance of preferred stock			(52,222)	
Proceeds and tax benefit from exercise of share based compensation		3,736		6,867
Purchase of treasury stock		(12,482)		(45,992)
Cash dividends paid		(4,154)		(12,493)
Net cash (used in) provided by financing activities	(625)	184,100	1,292,473	145,382
NET CHANGE IN CASH AND CASH EQUIVALENTS				
CASH AND CASH EQUIVALENTS Beginning of period				
CASH AND CASH EQUIVALENTS End of period	$	$	$	$

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MONEYGRAM INTERNATIONAL, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS DEFICIT
UNAUDITED

(Amounts in thousands, except share data)	Common Stock	Additional Capital	Retained Loss	Unearned Employee Benefits and Other	Accumulated Other Comprehensive Loss	Common Stock in Treasury	Total
December 31, 2007	$886	$ 73,077	$(387,479)	$(3,280)	$(21,715)	$(150,006)	$(488,517)
Cumulative adjustment for SFAS No. 158 - change of measurement date			(390)		(1,467)		(1,857)
Net loss			(384,246)				(384,246)
Reclassification of embedded derivative liability		70,827					70,827
Dividends on B and B-1 Preferred Stock		(50,810)					(50,810)
Accretion of preferred stock		(5,192)					(5,192)
Employee benefit plans		3,309		2,587		(2,555)	3,341
Unrealized foreign currency translation adjustment					1,273		1,273
Unrealized loss on available-for-sale securities					(8,932)		(8,932)
Reclassification of unrealized losses on derivative financial instruments					19,908		19,908
Amortization of prior service cost for pension and postretirement benefits, net of tax					296		296
Amortization of unrealized losses on pension and postretirement benefits, net of tax					645		645
September 30, 2008	$886	$ 91,211	$(772,115)	$ (693)	$ (9,992)	$(152,561)	$(843,264)

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MONEYGRAM INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Basis of Presentation

The accompanying unaudited consolidated financial statements of MoneyGram International, Inc. (MoneyGram or the Company) have been prepared in accordance with accounting principles generally accepted in the United States of America and the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and notes required for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included and are of a normal recurring nature. Operating results for the three and nine months ended September 30, 2008 are not necessarily indicative of the results that may be expected for future periods. For further information, refer to the Consolidated Financial Statements and Notes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2007.

2. Capital Transaction

The Company completed a capital transaction on March 25, 2008 pursuant to which the Company received $1.5 billion of gross equity and debt capital (the Capital Transaction) to support the long-term needs of the business and provide necessary capital due to the Company s investment portfolio losses described in Note 4 *Investment Portfolio*. The net proceeds of the Capital Transaction have been invested in cash and cash equivalents to supplement the Company s unrestricted assets. In connection with the Capital Transaction, the Company capitalized $107.5 million of transaction costs, including $7.5 million of costs paid through the issuance of Series B-1 Participating Convertible Preferred Stock (the B-1 Stock). See Note 9 *Mezzanine Equity* and Note 12 *Debt* for further information regarding transaction costs.

Equity Capital The equity component of the Capital Transaction consisted of the private placement of 495,000 shares of Series B Participating Convertible Preferred Stock (the B Stock, and collectively with the B-1 stock, the Series B Stock) and 265,000 shares of B-1 Stock to affiliates of Thomas H. Lee Partners, L.P. (THL) and affiliates of Goldman, Sachs & Co. (Goldman Sachs, and collectively with THL, the Investors) for an aggregate gross purchase price of $760.0 million. As a result of the issuance of the Series B Stock the Investors had an equity interest of approximately 79 percent on March 25, 2008. See Note 9 *Mezzanine Equity* for further information regarding the Series B Stock.

Senior Facility As part of the Capital Transaction, the Company s wholly owned subsidiary MoneyGram Payment Systems Worldwide, Inc. (Worldwide) entered into a senior credit facility (the Senior Facility) of $600.0 million with various lenders and JPMorgan Chase Bank, N.A. (JPMorgan), as Administrative Agent for the lenders. The Senior Facility amended and restated the $350.0 million Amended and Restated Credit Agreement dated as of June 29, 2005, and includes an additional $250.0 million term loan. In connection with this transaction, the Company terminated its $150.0 million 364-Day Credit Agreement with JPMorgan. See Note 12 *Debt* for further information regarding the Senior Facility.

Second Lien Notes As part of the Capital Transaction, Worldwide issued $500.0 million of senior secured second lien notes to Goldman Sachs (the Notes), which will mature in March 2018. See Note 12 *Debt* for further information regarding the Notes.

Participation Agreement between the Investors and Wal-Mart Stores, Inc. On February 11, 2008, the Investors entered into a Participation Agreement (as amended on March 17, 2008) with Wal-Mart Stores, Inc. (Wal-Mart) in connection with the Capital Transaction. The Company is not a party to the Participation Agreement, which was negotiated solely between the Investors and Wal-Mart. Under the terms of the Participation Agreement, each Investor is obligated to pay Wal-Mart certain percentages of accumulated cash payments received by the Investors in excess of the Investors original investment in the Company. Cash payments include dividends paid by the Company to the Investors and any cash payments received by the Investors in connection with the sale of any shares of the Company s stock to an unaffiliated third party or upon redemption by the Company. Wal-Mart, in its sole discretion, may elect to receive payments in cash or equivalent shares of stock held by the Investors. In addition, through March 17, 2010, the Investors must receive Wal-Mart s consent prior to voting in favor of, consenting to, or selling shares in a transaction that would cause a change in control of the Company, as defined by the Participation Agreement.

The Company has no obligation to Wal-Mart or additional obligations to the Investors under the terms of the Participation Agreement. However, in accordance with Staff Accounting Bulletin (SAB) Topic 5-T, *Accounting for Expenses or Liabilities Paid by Principal Stockholders*, the Company will recognize the Participation Agreement in its consolidated financial statements as if the Company itself entered into the agreement with Wal-Mart. As Wal-Mart may elect to receive any payments under the Participation Agreement in cash, the agreement is accounted for as a liability award under Statement of Financial Accounting Standards (SFAS) No. 123(revised 2004), *Share-Based Payment* (SFAS No. 123(R)). Under SFAS No. 123(R), the Company will recognize a liability equal to the fair value of the Participation Agreement through a charge to the Consolidated Statements of (Loss) Income when it becomes probable that certain performance conditions will be met. When recorded, the liability will be remeasured each period until settlement, with changes in fair value recognized in the Consolidated Statements of (Loss) Income. Wal-Mart s ability to earn the award under the Participation Agreement is conditioned upon the

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Investors receiving cash payments related to its Series B Stock in excess of the Investors original investment in the Company. While it is probable that the performance conditions will be met at September 30, 2008, the fair value of the liability is zero at this time, as the Company s discount rate, based on its debt interest rates and credit rating, exceeds the dividend rate on the preferred stock.

3. Unrestricted Assets

Through its wholly owned subsidiary and licensed entity MoneyGram Payment Systems, Inc. (MPSI), the Company is regulated by various state agencies that generally require MPSI to maintain liquid assets and investments with a rating of A or higher in an amount generally equal to the payment service obligations (PSO) for those regulated payment instruments, namely teller checks, agent checks, money orders and money transfers. The regulatory requirements are similar to, but less restrictive than, the Company s unrestricted assets measure. The regulatory PSO measure varies by state, but in all cases is substantially lower than the Company s PSO as disclosed in the Consolidated Balance Sheets as the Company is not regulated by state agencies for PSO resulting from outstanding cashier s checks or for amounts payable to agents and brokers. As a result of the regulatory requirements, a significant amount of cash and cash equivalents, receivables and investments are restricted to satisfy the liability to pay the face amount of regulated PSO upon presentment. The Company is not regulated by state agencies for PSO resulting from outstanding cashier s checks; however, the Company restricts a portion of the funds related to these payment instruments due to contractual arrangements and Company policy. Assets restricted for regulatory or contractual reasons are not available to satisfy working capital or other financing requirements. The regulatory and contractual requirements do not require the Company to specify individual assets held to meet the Company s PSO, nor is the Company required to deposit specific assets into a trust, escrow or other special account. Rather, the Company must maintain a pool of liquid assets. Provided the Company maintains a total pool of liquid assets sufficient to meet its regulatory and contractual requirements, the Company is able to withdraw, deposit or sell its individual liquid assets at will with no prior notice, penalty or limitations.

Regulatory requirements also require MPSI to maintain positive net worth, with one state also requiring that MPSI maintain positive tangible net worth. As of September 30, 2008, MPSI was in compliance with regulatory requirements for all states. In July 2008, MPSI was informed by one state that it was contemplating the assessment of a fine for the period from December 31, 2007 through March 24, 2008 that MPSI was out of compliance with the tangible net worth requirement. The Company believes that any such fine will not be material to the Company s Consolidated Financial Statements.

The Company has unrestricted cash and cash equivalents, receivables and investments to the extent those assets exceed all payment service obligations. These amounts are generally available; however, management considers a portion of these amounts as providing additional assurance that regulatory requirements are maintained. The following table shows the total amount of unrestricted assets at September 30, 2008 and December 31, 2007, respectively. The Company had a shortfall in its unrestricted assets at December 31, 2007 due to the decline in the fair value of its investments. See Note 4 *Investment Portfolio* for further information on the fair value of the Company s investments.

(Amounts in thousands)	**September 30, 2008**	**December 31, 2007**
Cash and cash equivalents	$ 4,561,905	$ 1,552,949
Receivables, net	1,397,179	1,408,220
Trading investments	30,285	62,105
Available-for-sale investments	480,944	4,187,384
	6,470,313	7,210,658
Amounts restricted to cover payment service obligations	(6,101,759)	(7,762,470)
Excess (shortfall) in unrestricted assets	$ 368,554	$ (551,812)

4. Investment Port