ENTERPRISE FINANCIAL SERVICES CORP
Form 11-K
June 29, 2009

As filed with the Securities and Exchange Commission on June 29, 2009

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 11-K

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

For the fiscal year ended December 31, 2008

or

o **TRANSITION REPORT PURSUANT TO SECTION 15(d) OF THE SECURITIES EXCHANGE ACT OF 1933**

For the transition period from ________ to ________

Commission File No. 001-15373

A. Full title of the plan and the address of the plan, if different from that of the issuer named below:

EFSC INCENTIVE SAVINGS PLAN

B. Name of issuer of the securities held pursuant to the plan and the address of its principal executive office:

Enterprise Financial Services Corp

150 N. Meramec
St. Louis, Missouri 63105

EFSC INCENTIVE SAVINGS PLAN
FINANCIAL STATEMENTS
DECEMBER 31, 2008 and 2007

(With Report of Independent Registered Public Accounting Firm)

CONTENTS

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Audit Committee and Plan Administrator
EFSC Incentive Savings Plan

We have audited the accompanying statement of net assets available for benefits of the EFSC Incentive Savings Plan (the Plan) as of December 31, 2008 and 2007, and the related statement of changes in net assets available for benefits for the years then ended. These financial statements are the responsibility of the Plans management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Plans internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net assets available for benefits of the Plan as of December 31, 2008 and 2007, and the changes in net assets available for benefits for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 3 to the financial statements, the Plan adopted Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements*, as of January 1, 2008.

/s/ RubinBrown LLP
St. Louis, Missouri
June 29, 2009

EFSC INCENTIVE SAVINGS PLAN
STATEMENT OF NET ASSETS AVAILABLE FOR BENEFITS

	December 31, 2008	December 31, 2007
Assets:		
Cash	$ 69,145	$ 65,649
Investments, at fair value		
Mutual funds	8,216,395	12,033,480
Common/collective trust funds	1,151,060	712,296
Common stock fund	991,856	—
Common stock	—	1,863,252
Participant loans	212,636	257,740
Total Investments	10,571,947	14,866,768
Receivables		
Employer matching contribution receivables	425,148	441,878
Net Assets Available For Benefits	$ 11,066,240	$ 15,374,295

See the accompanying notes to financial statements.

EFSC INCENTIVE SAVINGS PLAN
STATEMENT OF CHANGES IN NET ASSETS
AVAILABLE FOR BENEFITS

	Years ended December 31, 2008	Years ended December 31, 2007
Additions:		
Contributions		
Salary deferral contributions	$ 1,680,714	$ 1,739,486
Employer matching contributions, net of forfeitures	425,148	441,878
Participant rollover contributions	58,556	221,235
Total Contributions	2,164,418	2,402,599
Total Additions	2,164,418	2,402,599
Deductions:		
Benefits paid to participants	1,451,310	2,072,903
Other expenses	1,326	1,683
Total Deductions	1,452,636	2,074,586
Investment (Loss) Income:		
Net change in fair value of investments	(5,491,615)	(689,865)
Dividend income	418,389	830,602
Interest income on common/collective trust funds	33,486	39,660
Interest income on participant loans	19,903	22,390
Net Investment (Loss) Income	(5,019,837)	202,787
Net (Decrease) Increase	(4,308,055)	530,800

Net Assets Available For Benefits - Beginning Of Year	15,374,295	14,843,495
Net Assets Available For Benefits - End Of Year	$ 11,066,240	$ 15,374,295

See the accompanying notes to financial statements.

EFSC INCENTIVE SAVINGS PLAN
NOTES TO FINANCIAL STATEMENTS
December 31, 2008 And 2007

NOTE 1 DESCRIPTION OF THE PLAN

The following description of the EFSC Incentive Savings Plan (the Plan) provides only general information. Participants should refer to the Plan Agreement for a complete description of the Plans provisions.

General

The Plan is a defined contribution plan, with a 401(k) provision, covering all employees of Enterprise Financial Services Corp and its wholly owned subsidiaries (excluding Millennium Brokerage Group, LLC) (Enterprise) who are not seasonal employees and have attained the age of 21. It is subject to the provisions of the Employee Retirement Income Security Act of 1974 (ERISA). On January 1, 2008, the Plan name was changed from Enterprise Bank Incentive Savings Plan to EFSC Incentive Savings Plan.

The Plan Administrator and Plan Sponsor is Enterprise Financial Services Corp. The Plan Trustee is Enterprise Bank Incentive Savings Plan Trustee Committee which is comprised of five employees of Enterprise. The Plan Trustee meets twice per Plan year.

Contributions

Participants may contribute from 1% to 75% of eligible compensation to the Plan on a pre-tax basis. Enterprise may also make an annual employer matching contribution which is discretionary and determined by the Board of Directors of Enterprise. The employer matching contribution, on behalf of each participant, will be a percentage of deferrals up to the first 5% of the participants compensation. Participants may also contribute qualified rollover contributions representing distributions from other qualified defined benefit or defined contribution plans. All contributions are subject to applicable limits of the Internal Revenue Code.

Employer matching contributions were $460,023 and $486,145 for 2008 and 2007, respectively.

Vesting

Participants are immediately vested in their contributions, including rollover contributions plus actual earnings thereon. Vesting in the remainder of their accounts is based on years of service, as defined in the Plan Agreement. Participants vest according to a five-year graded schedule and are 20% vested after one year of service and 100% vested after five years of service, upon reaching early or normal retirement, upon total and permanent disability or death.

Participant Accounts

Each participants account is credited with the participants contributions, the employers matching contributions and an allocation of the Plans earnings. The allocation of earnings is determined by the earnings of the participants investment selection based on each participants balance, as defined in the Plan Agreement. The benefit to which a participant is entitled is the benefit that can be provided from the participants vested account.

Payment of Benefits

While actively employed, participants may receive hardship withdrawals of their vested account balance, subject to applicable regulations and approvals covering hardship withdrawals. Also, participants age 65 and over may receive regular in-service distributions of their vested accounts while actively employed.

On termination of service, a participant may elect to defer their distribution or, subject to appropriate spousal consent, receive either a lump-sum distribution or a Qualified Joint and Survivor Annuity equal to the participants vested interest in their account. Account balances less than $5,000 are generally distributed to an Individual Retirement Arrangement (IRA) if the participant does not make a distribution election.

Forfeitures

Participants forfeit the nonvested portion of their accounts in the Plan upon termination of employment with Enterprise. As described in the Plan, forfeitures are used to reduce future employer matching contributions or administrative expenses of the Plan. Forfeitures used to offset employer matching contributions amounted to $34,875 and $44,267 for the years ended December 31, 2008 and 2007, respectively.

Participant Loans

Participants may borrow from their fund accounts a minimum of $1,000 up to a maximum of $50,000 or 50% of their vested account balance, whichever is less. Loan terms range from one month to five years (longer for the purchase of a primary residence), at a mutually agreed term between the participant and the Plan Administrator. The loans are secured by the vested balance in the participants account and bear interest at a rate commensurate with local prevailing rates as determined by the Plan Administrator. Principal and interest are paid through payroll deductions.

Administrative Expenses

Substantially all administrative expenses of the Plan are paid by Enterprise.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The accompanying financial statements are presented on the accrual basis of accounting.

Investment Valuation and Income Recognition

The Plans investments are stated at fair value. Mutual funds are valued at quoted market prices. Common/collective trust funds are reported at fair value. Common stock is valued at the last reported sales price on the last day of the Plan year. Participant loans are valued at cost, which approximates fair market value.

The EFSC Common Stock Fund (the Fund) was established on January 1, 2008 and is tracked on a unitized basis. The Fund consists primarily of Enterprise Financial Services Corp (EFSC) common stock, and also includes cash investments in the Charles Schwab Institutional Money Market Fund sufficient to meet the Funds daily liquidity needs. EFSC common stock is traded on a national securities exchange (NASDAQ: EFSC). The value of a unit reflects the combined market value of EFSC common stock and the cash investments held by the Fund. At December 31, 2008, 152,786 units were outstanding with a value of $6.49 per unit.

Purchases and sales of securities are recorded on a trade-date basis. Interest income is recorded on an accrual basis. Dividends are recorded on the ex-dividend date.

Fair Value Measurements

On January 1, 2008, the Plan adopted Financial Accounting Standards Board (FASB) Statement No. 157, *Fair Value Measurements*, and subsequently adopted certain related FASB staff positions. Refer to Note 3 for fair value measurements of the Plans investments.

Estimates and Assumptions

The preparation of 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, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of additions to and deductions from net assets during the reporting period. Actual results could differ from those estimates.

As described in Financial Accounting Standards Board Staff Position, *FSP AAG INV-1 and SOP 94-4-1, Reporting of Fully Benefit-Responsive Investment Contracts Held by Certain Investment Companies Subject to the AICPA Investment Company Guide and Defined-Contribution Health and Welfare and Pension Plans* (the FSP), investment contracts held by a defined contribution plan are required to be reported at fair value.

However, contract value is the relevant measurement attribute for that portion of the net assets available for benefits of a defined contribution plan attributable to fully benefit-responsive investment contracts because contract value is the amount participants would receive if they were to initiate permitted transactions under the terms of the Plan. The FSP requires that the statement of net assets available for benefits presents the fair value of the investment contracts as well as the adjustment of the fully benefit-responsive investment contracts from fair value to contract value. The adjustment to contract value is immaterial for 2008 and 2007. The statement of changes in net assets available for benefits is prepared on a contract-value basis.

Payment of Benefits

Benefits are recorded when paid.

Reclassification

Certain amounts in the 2007 financial statements were classified, where appropriate, to conform to the 2008 financial statement presentation.

NOTE 3 — INVESTMENTS

The Plan's investments are held in a qualified tax-exempt trust, managed by Charles Schwab Trust Company (the Custodian). Participants can direct contributions to any of 20 investment options offered by the Plan. On January 1, 2008, the Enterprise Financial Services Corp common stock held in the Plan was converted to a unitized common stock fund, the EFSC Common Stock Fund.

Investments that represent 5% or more of the Plan's net assets available for benefits at the beginning of each respective Plan year are summarized as follows:

	December 31,			
	2008		2007	
utual funds:				
BlackRock Small Cap Growth Equity Portfolio - Institutional Share Class (added April 4, 2008)	$ 458,529		$ —	
Cohen & Steers Realty Shares, Inc. (added April 4, 2008)	22,933		—	
CRM Mid-Cap Value Fund - Institutional Shares	619,360		1,013,406	**
Davis New York Venture Shares - Class A Shares	698,808		1,150,252	**
Dodge and Cox Stock Fund	596,581		786,547	**
American Funds EuroPacific Growth Fund, Class A Shares	1,015,222	**	1,500,662	**
American Funds The Growth Fund of America, R4	1,128,326	**	1,722,866	**
PIMCO Total Return Fund - Administrative Class	1,324,283	**	1,356,432	**
Third Avenue Small-Cap Value Fund	570,950		793,481	**
Turner Mid-Cap Growth Fund, Investor Class Shares	469,672		826,850	**
Trendstar Small-Cap Fund (removed April 4, 2008)	—		810,076	**
Tweedy Browne Global Value Fund	533,837		761,745	**
Vanguard 500 Index Fund, Signal Shares	777,894	**	1,311,163	**
ommon/collective trust funds:				
Federated Capital Preservation Fund - ISP Share Class	763,479		712,296	
Schwab Managed Retirement Trust Income Fund Class III (added December 27, 2007)	—		—	
Schwab Managed Retirement Trust 2010 Fund Class III (added December 27, 2007)	27		—	
Schwab Managed Retirement Trust 2020 Fund Class III (added December 27, 2007)	261,720		—	
Schwab Managed Retirement Trust 2030 Fund Class III (added December 27, 2007)	92,530		—	
Schwab Managed Retirement Trust 2050 Fund Class III (added December 27, 2007)	26,409		—	

Schwab Managed Retirement Trust 2040 Fund Class III (added December 27, 2007)	6,895		—	
mmon stock fund:				
EFSC Common Stock Fund	991,856	**	—	
mmon stock:				
Enterprise Financial Services Corp (NASDAQ: EFSC) (converted to the EFSC Common Stock Fund on January 1, 2008)	—		1,863,252	n
rticipant loans	212,636		257,740	

n Nonparticipant directed investment

** Represented 5% or more of the Plan's net assets available for benefits.
All other amounts included for comparison purposes only.

The Plan's investments (including gains and losses in investments bought and sold, as well as held during the year) depreciated in value as follows for the years ended December 31:

	Years ended December 31, 2008	2007
Mutual funds	$ (4,729,595)	$ 105,916
Common/collective trust funds	(144,026)	—
Common stock fund and common stock	(617,994)	(795,781)
	$ (5,491,615)	$ (689,865)

Information about the assets and the significant components of the changes in assets relating to nonparticipant-directed investments follows:

	For The Years Ended December 31, 2008	2007
Assets:		
Enterprise Financial Services Corp common stock, 0 and 78,255 shares, respectively	**$** —	$ 1,863,252
Changes in assets:		
Employer contributions	**$** —	
Net transfers to participants-directed investments	(1,080,372)	
Interest and dividend income	14,682	
Benefits paid	(179,568)	
Depreciation in fair value of investments	(617,994)	
	$ (1,863,252)	

On January 1, 2008, a common stock fund containing Enterprise Financial Services Corp common stock was added as a participant-directed investment. The Enterprise Financial Services Corp common stock in the Plan as of December 31, 2007 was from company matches in 2001 through 2005. These shares were unitized and transferred to the common stock fund on January 1, 2008. In 2007, the Plan implemented rules relating to the Pension Protection Act of 2006, which required plans to allow participants the option to diversify from employer stock. Prior to the creation of the EFSC Common Stock Fund, participants were not allowed to buy into the

Enterprise Financial Services Corp common stock in the Plan.

Fair Value Measurements

Effective January 1, 2008 the Plan adopted FASB Statement No. 157, *Fair Value Measurement*, (FAS 157) which establishes a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy under FAS 157 are described below.

- *Level 1 Inputs* Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Plan has the ability to access.

- *Level 2 Inputs* Inputs to the valuation methodology include:
  - Quoted prices for similar assets or liabilities in active markets;
  - Quoted prices for identical or similar assets or liabilities in inactive markets;
  - Inputs other than quoted prices that are observable for the asset or liability;
  - Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

- *Level 3 Inputs* — Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset’s or liability’s fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at December 31, 2008 and 2007.

- Mutual funds — Valued at the net asset value (NAV) of shares held by the Plan at year end.
- Common/collective trust funds — Valued at fair value with the exception of the Federated Capital Preservation Fund, which is stated at contract value. The contract value of the Federated Capital Preservation Fund closely approximated fair value.
- Common stock fund — Valued at the closing price reported on the active market on which the individual securities are traded.
- Participant loans — Valued at their outstanding balances, which approximates fair value.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Plan Administrator believes the valuation methods are appropriate and consistent with those used by other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The following table sets forth by level, within the fair value hierarchy, the Plan’s assets at fair value as of December 31, 2008.

	Fair Value Measurements using Input Type			
	Level 1	Level 2	Level 3	Total
Mutual funds	$ 8,216,395	$ —	$ —	$ 8,216,395
Common/collective trust funds	—	1,151,060	—	1,151,060
Common stock fund	—	991,856	—	991,856
Participant loans	—	—	212,636	212,636

Total investments at fair value	$	8,216,395	$	2,142,916	$	212,636	$	10,571,947

The table below sets forth a summary of changes in the fair value of the Plan's level 3 assets for the year ended December 31, 2008.

		Level 3 Assets Participant Loans
Balance at January 1, 2008	$	257,740
Issuances, repayments and settlements, net		(45,104)
Balance at December 31, 2008	$	212,636

NOTE 4 — PLAN TERMINATION

Although it has not expressed intent to do so, Enterprise has the right under the Plan to discontinue its contributions at any time and to terminate the Plan, subject to the provisions of ERISA. In the event of Plan termination, participants will become 100% vested in their accounts. Enterprise may elect to have all assets transferred to another qualified plan in which all participants who would have otherwise received a distribution will have an interest, and each participant's interest will be nonforfeitable as to amounts attributable to assets transferred on his or her behalf.

NOTE 5 — INCOME TAX STATUS

The Plan received a favorable determination letter dated August 7, 2001 from the Internal Revenue Service stating that the Plan, as designed, is in compliance with the applicable requirements of the Internal Revenue Code. The Plan Sponsor amended and restated the Plan effective January 1, 2003 by adopting the Retirement Plan Services, LLC prototype document. The Plan Administrator believes that the Plan is qualified and the related trust is tax-exempt.

Currently, the Plan Administrator is working with the Plan's counsel to correct certain operational failures of the Plan. The Plan Administrator will submit the corrections for approval through the Internal Revenue Service's voluntary correction program. The Plan Administrator believes that the corrective actions will maintain the tax qualified status of the Plan and the related trust will continue to be tax-exempt.

NOTE 6 — TRANSACTIONS WITH PARTIES-IN-INTEREST

During 2008 and 2007, the Plan purchased 87,635 and 7,024 EFSC common shares, respectively. The Plan also sold or distributed a total of 24,244 and 20,203 EFSC common shares, during 2008 and 2007, respectively. All shares were bought or sold on the open market.

Enterprise owns a 10% membership interest in Retirement Plan Services, LLC, the Plan's third-party recordkeeper.

The investment advisor for the Plan is Moneta Group, a nationally recognized firm in the financial planning industry. In 1997, Enterprise entered into a solicitation and referral agreement with Moneta Group. Certain Moneta Group employees have been granted stock options under this referral agreement for EFSC common stock which can be exercised through 2013. The number of outstanding stock options held by Moneta Group at December 31, 2008 was 91,001. There have been no stock options issued to Moneta Group employees since 2003.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON SUPPLEMENTARY INFORMATION

Our audits were performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental schedule of assets held at end of year is presented for purposes of additional analysis and is not a required part of the basic financial statements, but is supplementary information required by the

Department of Labor's Rules and Regulations for Reporting and Disclosure under the Employee Retirement Income Security Act of 1974. This supplemental schedule is the responsibility of the Plan's management. The supplemental schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

/s/ RubinBrown LLP
St. Louis, Missouri
June 29, 2009

EFSC INCENTIVE SAVINGS PLAN
SUPPLEMENTAL SCHEDULE

EIN: 43-1706259 PLAN: 001
SCHEDULE OF ASSETS HELD AT END OF YEAR
December 31, 2008

Identity of issuer, borrower, lessor or similar party	Description of investment, including maturity date, collateral and maturity value
Mutual funds:	
BlackRock Small Cap Growth Equity Portfolio - Institutional Share Class	
Cohen & Steers Realty Shares, Inc.	
CRM Mid-Cap Value Fund - Institutional Shares	
Davis New York Venture Shares - Class A Shares	
Dodge and Cox Stock Fund	
American Funds EuroPacific Growth Fund, Class A Shares	
American Funds The Growth Fund of America, R4	
PIMCO Total Return Fund - Administrative Class	
Third Avenue Small-Cap Value Fund	
Turner Mid-Cap Growth Fund, Investor Class Shares	
Trendstar Small-Cap Fund	
Tweedy Browne Global Value Fund	
Vanguard 500 Index Fund, Signal Shares	
Common/collective trust funds:	
Federated Capital Preservation Fund - ISP Share Class	
Schwab Managed Retirement Trust Income Fund Class III	
Schwab Managed Retirement Trust 2010 Fund Class III	
Schwab Managed Retirement Trust 2020 Fund Class III	
Schwab Managed Retirement Trust 2030 Fund Class III	
Schwab Managed Retirement Trust 2050 Fund Class III	
Schwab Managed Retirement Trust 2040 Fund Class III	
Common stock fund:	
EFSC Common Stock Fund *	
Participant loans	Interest rates ranging from 5.00% to 10.00%; Due at various dates through 2035
Total Investments	

* Represents a party-in-interest to the Plan.

The above information is a required disclosure for IRS Form 5500, Schedule H, Part IV, line 4i.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Plan Trustees or other persons who administer the employee benefit plan) has duly caused this annual report to be signed on its behalf by the undersigned hereunto duly authorized.

Date: June 29, 2009

EFSC Incentive Savings Plan

/s/ Deborah N. Barstow
Deborah N. Barstow
Senior Vice President & Controller
Enterprise Financial Services Corp

EXHIBIT INDEX

Exhibit No.	Description
23	Consent of Independent Registered Public Accounting Firm

IZE="2">$1,154.2

CASH FLOWS FROM OPERATING ACTIVITIES

Net (loss) income from continuing operations

(382.3) 400.6

Net income from discontinued operations

3.5

Adjustments to reconcile to net cash provided by operating activities:

Depreciation and amortization (including amortization netted against equity earnings in affiliates and revenues)

761.9 365.0

Charges (gains) related to restructuring, impairments, litigation and regulatory settlements, other and other income (expense)

36.7 18.1

Other non-cash and non-operating items, net

(30.0) (85.4)

Increase (decrease) in cash, excluding the effects of acquisitions and dispositions, resulting from changes in:

Accounts receivable, current and long-term

162.9 (35.6)

Other assets, current and long-term

188.4 28.0

Accounts payable and other liabilities, current and long-term

(227.2) (87.2)

Income tax accounts

(213.8) 61.3

Excess tax benefit from share-based payment arrangement

(28.7)

Net cash provided by operating activities from continuing operations

296.6 636.1

Net cash used in operating activities from discontinued operations

(9.7)

Net cash provided by operating activities

296.6 626.4

CASH FLOWS FROM INVESTING ACTIVITIES

Current period acquisitions, net of cash acquired

(195.4) (369.7)

Payments related to other businesses previously acquired

(16.7) (49.3)

Additions to property and equipment, net

(122.6) (116.4)

Payments to secure customer service contracts, including outlays for conversion, and capitalized systems development costs

(77.1) (70.3)

Proceeds from the sale of marketable securities

52.4 11.2

Other investing activities

5.0 56.1

Net cash used in investing activities

(354.4) (538.4)

CASH FLOWS FROM FINANCING ACTIVITIES

Short-term borrowings, net

61.0 (57.0)

Principal payments on long-term debt

(97.2) (115.5)

Proceeds from issuance of common stock

129.0

Capital contributed by Parent

104.3

Excess tax benefit from share-based payment arrangement

28.7

Purchase of treasury shares

(278.2)

Cash dividends

(0.9) (45.2)

Net cash provided by (used in) financing activities

67.2 (338.2)

Effect of exchange rate changes on cash and cash equivalents

39.4 20.5

Change in cash and cash equivalents

48.8 (229.7)

Cash and cash equivalents at end of period	$655.3	$924.5

See Notes to Consolidated Financial Statements.

FIRST DATA CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1: Basis of Presentation

The accompanying Consolidated Financial Statements of First Data Corporation (FDC or the Company) should be read in conjunction with the Company s Annual Report on Form 10-K for the year ended December 31, 2007. Significant accounting policies disclosed therein have not changed.

On September 24, 2007, the Company was acquired through a merger transaction (the merger) with an entity controlled by affiliates of Kohlberg Kravis Roberts & Co. (KKR or the sponsor). The merger resulted in the equity of FDC becoming privately held. Details of the merger are more fully discussed in Note 3. The accompanying consolidated statements of operations and cash flows are presented for two periods: predecessor (the three and six month periods ended June 30, 2007) and successor (the three and six month periods ended June 30, 2008), which relate to the periods preceding the merger and the periods succeeding the merger, respectively. The Company applied purchase accounting to the opening balance sheet and results of operations on September 25, 2007 as the merger occurred at the close of business on September 24, 2007. The merger resulted in a new basis of accounting beginning on September 25, 2007.

The accompanying Consolidated Financial Statements are unaudited; however, in the opinion of management, they include all normal recurring adjustments necessary for a fair presentation of the consolidated financial position of the Company at June 30, 2008, and the consolidated results of its operations and cash flows for the successor and predecessor periods for the three and six months ended June 30, 2008 and 2007, respectively. Results of operations reported for interim periods are not necessarily indicative of results for the entire year due in part to the seasonality of certain business units.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the Consolidated Financial Statements and accompanying notes. Actual results could differ from these estimates.

Presentation

The Company s Consolidated Balance Sheet presentation has historically been unclassified due to the short-term nature of its settlement obligations contrasted with the Company s ability to invest cash awaiting settlement in long-term investment securities. The Company repositioned the majority of its investment portfolio associated with cash awaiting settlement from long-term investments to short-term investments. As a result of the repositioning of the portfolio such that a majority of the settlement assets and all settlement liabilities are short-term, the Company has changed to a classified balance sheet. The Consolidated Balance Sheet as of December 31, 2007 has been revised to conform to this presentation.

A new Chief Executive Officer, the Company s chief operating decision maker, was appointed as a result of the September 24, 2007 merger with an affiliate of KKR. In connection with this change in leadership, changes were made to the Company s senior management and organization of the business. Effective January 1, 2008, the Company s new Chief Executive Officer began making strategic and operating decisions with regards to assessing performance and allocating resources based on a new segment structure. Segment results for 2007 have been revised to reflect the new structure. In connection with this segment realignment, the Company also reclassified certain transaction and processing service fee revenue components in the Consolidated Statements of Operations, primarily the prepaid business from Merchant related services to Other services and the debit network business from Merchant related services to Card services . Additionally, consolidated expenses for 2007 have been revised to present certain depreciation and amortization amounts as a separate component of expenses.

Official Check and Money Order Wind-down

In conjunction with the wind-down of the official check and money order business (included within the Integrated Payment Systems (IPS) segment) and in the first quarter 2008, the Company repositioned its investment portfolio to principally taxable investments. As a result, the revenues and operating profit of the IPS segment are no longer stated on a pretax equivalent basis effective as of January 1, 2008. The investment portfolio decreased from $12.6 billion at December 31, 2007 to $6.3 billion at June 30, 2008 due to the wind-down. The investment portfolio included approximately $541 million of student loan auction rate securities as of June 30, 2008 compared to approximately $1,077 million as of December 31, 2007. The auction mechanism on these investments failed subsequent to December 31, 2007 so investments held at

June 30, 2008 are not currently liquid; however, all of the securities are AAA rated, except for one AA rated and are collateralized by securitized student loans substantially guaranteed by

FIRST DATA CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

the United States Government. The Company has the ability and intent to hold them for an extended period during which the Company anticipates an auction mechanism or an alternative liquidity vehicle will be established. Due to the lack of observable market activity for the Company s student loan auction rate securities, they have been valued based on comparison to similar securities for which market data is available. The Company has recorded an unrealized loss of $12.1 million in Other Comprehensive Income which it attributes to limited liquidity rather than credit issues.

In July 2008, IPS agreed with The Western Union Company (Western Union) that on October 1, 2009 IPS will assign and transfer to Western Union, among other things, certain assets and equipment used by IPS to issue retail money orders and an amount sufficient to satisfy all outstanding retail money orders. On the closing date, Western Union will assume IPS s role as issuer of the retail money orders. The transfer will result in a significant decrease to the IPS settlement asset portfolio.

Revenue Recognition

The Company recognizes revenues from its processing services as such services are performed. Revenue is recorded net of certain costs such as credit and offline debit interchange fees and assessments charged by credit card associations which totaled $2,164.1 million and $1,829.6 million for the three months ended June 30, 2008 and 2007, respectively and $4,089.2 million and $3,481.4 million for the comparable six-month periods. Debit network fees related to acquired PIN-based debit transactions are recognized in the Reimbursable debit network fees, postage and other revenue and expense lines of the Consolidated Statements of Operations. The debit network fees related to acquired PIN-debit transactions charged by debit networks totaled $327.2 million and $254.7 million for the three months ended June 30, 2008 and 2007, respectively and $613.1 million and $479.6 million for the comparable six-month periods.

New Accounting Pronouncements

In December 2007, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 141(R), Business Combinations. The new standard will significantly change the financial accounting and reporting of business combination transactions in the consolidated financial statements. It will require an acquirer to recognize, at the acquisition date, the assets acquired, the liabilities assumed, and any non-controlling interest in the acquiree at their full fair values as of that date. In a business combination achieved in stages (step acquisitions), the acquirer will be required to remeasure its previously held equity interest in the acquiree at its acquisition-date fair value and recognize the resulting gain or loss in earnings. The acquisition-related transaction and restructuring costs will no longer be included as part of the capitalized cost of the acquired entity but will be required to be accounted for separately in accordance with applicable generally accepted accounting principles. SFAS No. 141(R) applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008.

In December 2007, the FASB issued SFAS No. 160, Non-controlling Interests in Consolidated Financial Statements. The statement clarifies the definition of a non-controlling (or minority) interest and requires that non-controlling interests in subsidiaries be reported as a component of equity in the consolidated statement of financial position and requires that earnings attributed to the non-controlling interests be reported as part of consolidated earnings and not as a separate component of income or expense. However, it will also require expanded disclosures of the attribution of consolidated earnings to the controlling and non-controlling interests on the face of the consolidated income statement. SFAS No. 160 will require that changes in a parent s controlling ownership interest, that do not result in a loss of control of the subsidiary, are accounted for as equity transactions among shareholders in the consolidated entity therefore resulting in no gain or loss recognition in the income statement. Only when a subsidiary is deconsolidated will a parent recognize a gain or loss in net income. SFAS No. 160 is effective for fiscal years beginning on or after December 15, 2008, and will be applied prospectively except for the presentation and disclosure requirements that will be applied retrospectively for all periods presented.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

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Note 2: Supplemental Financial Information

The following table details the components of Other income (expense) on the Consolidated Statements of Operations:

(in millions)	Successor Three months ended June 30, 2008	Predecessor Three months ended June 30, 2007
Investment gains and (losses)	$	$ (0.1)
Derivative financial instruments gains and (losses)	9.4	
Divestitures, net		2.5
Non-operating foreign currency gains and (losses)	(3.0)	
Other income (expense)	$ 6.4	$ 2.4

(in millions)	Successor Six months ended June 30, 2008	Predecessor Six months ended June 30, 2007
Investment gains and (losses)	$ 22.1	$ (1.5)
Derivative financial instruments gains and (losses)	(3.4)	
Divestitures, net		3.5
Debt repayment gains and (losses)		1.4
Non-operating foreign currency gains and (losses)	(55.5)	
Other income (expense)	$ (36.8)	$ 3.4

The investment gains for the six months ended June 30, 2008 resulted from the sale of MasterCard stock. The derivative financial instruments gains and losses for the three and six month periods in 2008 were due most significantly to the mark-to-market adjustments for cross currency swaps, that are not designated as accounting hedges, and certain interest rate swaps that were not designated as accounting hedges for a period of time and the ineffectiveness from interest rate swaps that are designated as accounting hedges but are not perfectly effective.

For the three and six months ended June 30, 2008, the net non-operating foreign currency exchange losses related to the mark-to-market of the Company s intercompany loans and the euro-denominated debt issued in connection with the merger. Historically, intercompany loans were deemed to be of a long-term nature for which settlement was not planned or anticipated in the foreseeable future. Accordingly, the translation adjustments were reported in Other comprehensive income . Effective in September 2007 and in conjunction with the merger, the Company made the decision to begin settling intercompany loans which results in a benefit or charge to earnings due to movement in foreign currency exchange rates.

Supplemental Cash Flow Information

Significant non-cash transactions during the six months ended June 30, 2008 included the Company increasing the principal amount of its senior unsecured PIK term loan facility by $123.7 million resulting from the payment of interest expense. During the six months ended June 30, 2008, the Company entered into approximately $47 million of capital leases. Capital leases into which the Company entered during the six months ended June 30, 2007 were immaterial.

See Note 12 for information concerning the Company s stock-based compensation plans.

Note 3: Merger

On September 24, 2007, FDC merged with affiliates of KKR. For additional details, refer to Note 2 to the Consolidated Financial Statements in the Company s Annual Report on Form 10-K for the year ended December 31, 2007.

Preliminary Purchase Price Allocation

The total purchase price of approximately $26.6 billion was allocated to the Company s net tangible and identifiable intangible assets based on their estimated fair values as set forth below. A portion of the preliminary valuation of identifiable intangible assets was allocated to the Company s investments in unconsolidated joint ventures (reflected in the Investment in affiliates line of

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

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the Consolidated Balance Sheets). The excess of the purchase price over the net tangible and identifiable intangible assets was recorded as goodwill. The preliminary allocation of the purchase price to fixed assets and identifiable intangible assets was based upon preliminary valuation data and the estimates and assumptions are subject to change. The Company is also in the process of working through other potential purchase accounting adjustments that mostly relate to pre-acquisition contingencies and implementation of management s restructuring plans and related deferred taxes on the purchase accounting.

(in millions)	
Property and equipment	$ 1,063.2
Customer Relationships	6,390.9
Software	970.7
Tradenames	813.6
Other Intangibles	157.0
Goodwill	16,844.1
Investment in affiliates	3,729.7
Deferred taxes	(2,215.6)
Other net liabilities acquired	(1,175.8)
Total purchase price	$ 26,577.8

The preliminary estimated weighted-average useful lives (excluding the impact of accelerated amortization and the First Data tradename which was determined to have an indefinite life) associated with the intangible assets are approximately:

Customer Relationships	14 years
Software	6 years
Tradenames	12 years
Other Intangibles	16 years
Investment in affiliates	10 years
Total weighted-average useful lives	13 years

The Company generally uses straight-line amortization for intangible assets other than for customer relationships for which the pattern of economic benefits are known and for which an accelerated method of amortization is used to more appropriately allocate the cost of the relationships to the periods that will benefit from them. Deferred tax liabilities were recorded related to the allocation of the purchase price to intangible assets. Less than 5% of goodwill resulting from the merger is deductible for tax purposes at a local jurisdiction level. The preliminary allocation of goodwill by segment is as follows (in millions):

Merchant Services	$ 9,361.0
Financial Services	3,732.4
International	2,998.3
Prepaid Services	752.4
Integrated Payment Systems	
All Other and Corporate	
	$ 16,844.1

Goodwill will be reviewed at least annually for impairment.

Merger Related Restructuring Charges

During the fourth quarter 2007, the Company implemented a plan that provided strategic direction for the Company under its new leadership. The plan anticipated capturing efficiencies related to the simplification of domestic and international operations and other near term cost saving initiatives as well as certain reductions in personnel. In accordance with this plan and in November 2007, the Company terminated approximately 1,600 employees across the organization representing all levels of employees and approximately 6% of its worldwide work force. A majority of them ceased working before December 31, 2007. Additional actions

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

occurred during first and second quarters 2008 resulting in the termination of over 400 employees across the organization. A majority of the successor severance costs were recorded in purchase accounting with the remainder recorded through current operations. The Company anticipates taking additional similar types of actions during the remainder of 2008 as part of its overall plan, with the majority of severance costs to be recorded in purchase accounting as assumed liabilities.

The following table summarizes the Company s utilization of restructuring accruals related to the merger recorded in purchase accounting for the six months ended June 30, 2008:

(in millions)	**Employee Severance**
Remaining accrual at January 1, 2008	$ 92.4
Charges recorded in purchase accounting	37.0
Cash payments	(71.8)
Other adjustments	(1.5)
Remaining accrual at June 30, 2008	$ 56.1

Merger and Other Related Costs

During the three and six months ended June 30, 2007, the Company expensed merger related costs consisting primarily of investment banking, accounting and legal fees totaling $10.9 million and $15.9 million, respectively. During the three and six months ended June 30, 2008, the Company expensed $2.3 million and $5.3 million, respectively for similar costs.

Unaudited Pro Forma Condensed Consolidated Statements of Operations

The following Unaudited Pro Forma Condensed Consolidated Statements of Operations reflect the consolidated results of operations of the Company as if the merger had occurred on January 1, 2007. The historical financial information has been adjusted to give effect to events that are (1) directly attributed to the merger, (2) factually supportable, and (3) with respect to the statement of operations, expected to have a continuing impact on the combined results. Such items include interest expense related to debt issued in conjunction with the merger as well as additional amortization expense associated with the preliminary valuation of intangible assets. This unaudited pro forma information should not be relied upon as necessarily being indicative of the historical results that would have been obtained if the merger had actually occurred on that date, nor of the results that may be obtained in the future.

Unaudited Pro Forma Condensed Consolidated Statements of Operations

	Three months ended June 30, 2007 (in millions)	**Six months ended June 30, 2007 (in millions)**
Revenues:		
Transaction and processing service fees	$ 1,377.8	$ 2,645.5
Investment income, net	(7.5)	(37.8)
Product sales and other	199.5	387.5
Reimbursable debit network fees, postage and other	430.9	841.8

	2,000.7	3,837.0
Expenses:		
Cost of services (exclusive of items shown below)	717.6	1,406.4
Cost of products sold	72.9	139.6
Selling, general and administrative	324.1	618.0
Reimbursable debit network fees, postage and other	430.9	841.8
Depreciation and amortization	300.6	600.6
Other operating expenses:		
Restructuring, net	5.9	7.9
Impairments		16.3
Litigation and regulatory settlements	5.0	5.0

FIRST DATA CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

	Three months ended June 30, 2007 (in millions)	Six months ended June 30, 2007 (in millions)
Other	(7.7)	(7.7)
	1,849.3	3,627.9
Operating profit	151.4	209.1
Interest income	12.9	20.9
Interest expense	(485.1)	(995.2)
Other income (expense)	2.4	2.0
	(469.8)	(972.3)
Loss before income taxes, minority interest, equity earnings in affiliates and discontinued operations	(318.4)	(763.2)
Income taxes	(162.6)	(371.7)
Minority interest	(40.0)	(69.1)
Equity earnings in affiliates	33.5	55.6
Loss from continuing operations	$ (162.3)	$ (405.0)

Note 4: Restructuring, Impairments, Litigation and Regulatory Settlements and Other

Restructuring charges and reversal of restructuring accruals

The Company recorded restructuring charges in 2007 comprised of severance totaling $6.7 million and $9.5 million for the three and six months ended June 30, 2007. Severance charges resulted from the termination of approximately 350 employees within the Merchant Services and the International segments.

Restructuring charges for first quarter 2007 resulted from efforts to improve the overall efficiency and effectiveness of the sales and sales support teams within the Merchant Services segment. Severance charges resulted from the termination of approximately 230 sales related employees comprising approximately 10% of the segment s regional sales, cross-sale and sales support organizations. This restructuring plan was completed in the first quarter of 2007. Restructuring charges for the second quarter 2007 resulted from the termination of approximately 120 employees within the International segment. These were the first of the terminations that occurred associated with data center consolidation and global sourcing initiatives. Similar actions will occur in future periods. The Company also reversed $0.8 million and $1.6 million for the three and six months ended June 30, 2007, respectively, of prior period restructuring accruals related to changes in estimates regarding severance costs from restructuring activities that occurred in 2005 and 2006.

The following table summarizes the Company s utilization of restructuring accruals from continuing operations, excluding merger related restructuring charges described in Note 3, for the period from January 1, 2008 through June 30, 2008 (in millions):

	Employee Severance	Facility Closure

Remaining accrual at January 1, 2008	$	6.5	$	0.1
Expense provision				
Cash payments and other		(2.9)		(0.1)
Changes in estimates [(a)]		(0.9)		
Remaining accrual at June 30, 2008	$	2.7	$	