MASTERCARD INC
Form 10-Q
May 01, 2009
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended March 31, 2009

Or

¨ **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: 001-32877

MasterCard Incorporated

(Exact name of registrant as specified in its charter)

Delaware	**13-4172551**
(State or other jurisdiction of incorporation or organization)	***(IRS Employer Identification Number)***

2000 Purchase Street
Purchase, NY
(Address of principal executive offices)

10577
(Zip Code)

(914) 249-2000

(Registrant s telephone number, including area code)

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 ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ¨ No ¨

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 x	Accelerated filer ¨
Non-accelerated filer ¨	Smaller reporting company ¨
(do not check if a smaller reporting company)	

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

As of April 27, 2009, there were 98,515,734 shares outstanding of the registrant s Class A common stock, par value $.0001 per share, 30,848,778 shares outstanding of the registrant s Class B common stock, par value $.0001 per share, and 1,772 shares outstanding of the registrant s Class M common stock, par value $.0001 per share.

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MASTERCARD INCORPORATED

CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

	March 31, 2009	December 31, 2008
	(In thousands, except share data)	
ASSETS		
Cash and cash equivalents	$ 1,678,192	$ 1,505,160
Investment securities, at fair value:		
Available-for-sale	597,669	588,095
Municipal bonds held-to-maturity		154,000
Accounts receivable	533,654	639,482
Income taxes receivable		198,308
Settlement due from customers	554,624	513,191
Restricted security deposits held for customers	205,262	183,245
Prepaid expenses	206,572	213,612
Deferred income taxes	257,577	283,795
Other current assets	73,350	32,619
Total Current Assets	4,106,900	4,311,507
Property, plant and equipment, at cost (less accumulated depreciation of $289,634 and $278,269)	454,227	306,798
Deferred income taxes	553,338	567,567
Goodwill	281,277	297,993
Other intangible assets (less accumulated amortization of $376,759 and $377,570)	375,512	394,282
Investment securities available-for-sale, at fair value	191,240	191,760
Municipal bonds held-to-maturity	36,909	37,450
Prepaid expenses	316,381	302,095
Other assets	99,528	66,397
Total Assets	$ 6,415,312	$ 6,475,849
LIABILITIES AND EQUITY		
Accounts payable	$ 262,622	$ 262,342
Settlement due to customers	530,842	532,237
Restricted security deposits held for customers	205,262	183,245
Obligations under litigation settlements (Note 14)	710,735	713,035
Accrued expenses	898,228	1,032,061
Short-term debt		149,380
Other current liabilities	143,615	118,151
Total Current Liabilities	2,751,304	2,990,451
Deferred income taxes	69,436	74,518
Obligations under litigation settlements (Note 14)	898,875	1,023,263
Long-term debt	18,407	19,387
Other liabilities	447,961	436,255
Total Liabilities	4,185,983	4,543,874
Commitments and Contingencies (Notes 13, 14 and 16)		
Stockholders Equity		
Class A common stock, $.0001 par value; authorized 3,000,000,000 shares, 105,255,954 and 105,126,588 shares issued and 98,515,364 and 98,385,998 outstanding, respectively	10	10
Class B common stock, $.0001 par value; authorized 1,200,000,000 shares, 30,848,778 issued and outstanding, respectively	4	4
Class M common stock, $.0001 par value; authorized 1,000,000 shares, 1,765 and 1,728 shares issued and outstanding, respectively		
Additional paid-in-capital	3,320,352	3,304,604

Class A treasury stock, at cost, 6,740,590 shares, respectively	(1,250,000)	(1,250,000)
Retained earnings (accumulated deficit)	111,477	(236,100)
Accumulated other comprehensive income:		
Cumulative foreign currency translation adjustments	99,662	175,040
Defined benefit pension and other postretirement plans, net of tax	(42,166)	(43,207)
Investment securities available-for-sale, net of tax	(17,977)	(22,996)
Total accumulated other comprehensive income	39,519	108,837
Total Stockholders Equity	2,221,362	1,927,355
Non-controlling interests	7,967	4,620
Total Equity	2,229,329	1,931,975
Total Liabilities and Equity	$ 6,415,312	$ 6,475,849

The accompanying notes are an integral part of these consolidated financial statements.

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MASTERCARD INCORPORATED

CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)

	Three Months Ended March 31, 2009	2008
	(In thousands, except per share data)	
Revenues, net	$ 1,156,102	$ 1,182,084
Operating Expenses		
General and administrative	447,853	461,625
Advertising and marketing	115,969	179,588
Depreciation and amortization	30,987	25,264
Total operating expenses	594,809	666,477
Operating income	561,293	515,607
Other Income (Expense)		
Investment income, net	17,401	114,770
Interest expense	(35,798)	(15,318)
Other income, net	6,982	73,522
Total other income (expense)	(11,415)	172,974
Income before income taxes	549,878	688,581
Income tax expense	182,668	241,703
Net income	367,210	446,878
Loss attributable to non-controlling interests	48	
Net Income Attributable to MasterCard	$ 367,258	$ 446,878
Basic Earnings per Share (Note 2)	$ 2.81	$ 3.37
Basic Weighted Average Shares Outstanding (Note 2)	129,636	131,426
Diluted Earnings per Share (Note 2)	$ 2.80	$ 3.37
Diluted Weighted Average Shares Outstanding (Note 2)	129,975	131,764

The accompanying notes are an integral part of these consolidated financial statements.

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MASTERCARD INCORPORATED

CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

	Three Months Ended March 31, 2009	Three Months Ended March 31, 2008
	(In thousands)	
Operating Activities		
Net income	$ 367,210	$ 446,878
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	30,987	25,264
Gain on sale of Redecard S.A. available-for-sale securities		(85,903)
Share based payments (Note 12)	14,596	11,051
Stock units settled in cash for taxes	(7,253)	(65,760)
Tax benefit for share based compensation	(7,962)	(40,661)
Impairment of assets	15,258	7,309
Accretion of imputed interest on litigation settlements	25,612	7,982
Deferred income taxes	40,311	(31,982)
Other	(2,318)	2,550
Changes in operating assets and liabilities:		
Trading securities		2,561
Accounts receivable	101,517	16,369
Income taxes receivable	190,000	
Settlement due from customers	(69,438)	(20,861)
Prepaid expenses, current	4,076	(28,280)
Other current assets	(65,817)	(12,122)
Prepaid expenses, non-current	(23,497)	1,679
Litigation settlement payments	(152,300)	
Accounts payable	2,921	10,046
Settlement due to customers	31,557	(46,381)
Accrued expenses	(106,545)	(5,994)
Net change in other assets and liabilities	27,168	30,167
Net cash provided by operating activities	416,083	223,912
Investing Activities		
Purchases of property, plant and equipment	(11,932)	(12,447)
Capitalized software	(15,962)	(19,279)
Purchases of investment securities available-for-sale	(15,334)	(385,048)
Proceeds from sales and maturities of investment securities, available-for-sale	12,707	640,920
Investment in affiliates	(17,789)	(2,624)
Acquisition of business, net of cash acquired	(2,913)	
Other investing activities	1,693	514
Net cash provided by (used in) investing activities	(49,530)	222,036
Financing Activities		
Dividends paid	(19,676)	(20,038)
Cash proceeds from exercise of stock options	431	1,671
Tax benefit for share based compensation	7,962	40,661
Purchase of treasury stock		(294,112)

Payment of debt	(149,380)	
Redemption of non-controlling interest	(4,620)	
Net cash used in financing activities	(165,283)	(271,818)
Effect of exchange rate changes on cash and cash equivalents	(28,238)	39,125
Net increase in cash and cash equivalents	173,032	213,255
Cash and cash equivalents beginning of period	1,505,160	1,659,295
Cash and cash equivalents end of period	$ 1,678,192	$ 1,872,550

The accompanying notes are an integral part of these consolidated financial statements.

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MASTERCARD INCORPORATED

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(UNAUDITED)

	Total	Common Shares Class A	Common Shares Class B	Additional Paid-In Capital	Treasury Stock	Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Income, net of tax	Non-Controlling Interests
	(In thousands, except per share data)							
Balance at December 31, 2008	$ 1,931,975	$ 10	$ 4	$ 3,304,604	$ (1,250,000)	$ (236,100)	$ 108,837	$ 4,620
Redemption of non-controlling interest	(4,620)							(4,620)
Investment in majority owned entity	8,015							8,015
Net income (loss)	367,210					367,258		(48)
Other comprehensive loss, net of tax	(69,318)						(69,318)	
Cash dividends declared on Class A and Class B common stock, $0.15 per share	(19,669)			12		(19,681)		
Share based payments	14,596			14,596				
Stock units settled in cash for taxes	(7,253)			(7,253)				
Tax benefit for share based compensation	7,962			7,962				
Cash proceeds from exercise of stock options	431			431				
Balance at March 31, 2009	$ 2,229,329	$ 10	$ 4	$ 3,320,352	$ (1,250,000)	$ 111,477	$ 39,519	$ 7,967

MASTERCARD INCORPORATED

CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE INCOME

(UNAUDITED)

	Three Months Ended March 31, 2009	Three Months Ended March 31, 2008
	(In thousands)	
Net Income	$ 367,210	$ 446,878
Other comprehensive income (loss):		
Foreign currency translation adjustments	(75,378)	76,634
Defined benefit pension and postretirement plans, net of tax	1,041	141
Unrealized gain (loss) and reclassification adjustment for realized (gain) loss on investment securities available-for-sale, net of tax	5,019	(66,540)
Other comprehensive income (loss)	(69,318)	10,235
Comprehensive Income	297,892	457,113
Loss attributable to non-controlling interests	48	
Comprehensive Income Attributable to MasterCard	$ 297,940	$ 457,113

The accompanying notes are an integral part of these consolidated financial statements.

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MASTERCARD INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(In thousands, except percent and per share data)

Note 1. Summary of Significant Accounting Policies

Organization MasterCard Incorporated and its consolidated subsidiaries, including MasterCard International Incorporated (MasterCard International) and MasterCard Europe sprl (MasterCard Europe) (together, MasterCard or the Company), provide payment solutions, including transaction processing and related services to customers principally in support of their credit, deposit access (debit), electronic cash and Automated Teller Machine (ATM) payment card programs, and travelers cheque programs. Our financial institution customers are generally either principal members (principal members) of MasterCard International, which participate directly in MasterCard International s business, or affiliate members of MasterCard International, which participate indirectly in MasterCard International s business through a principal member.

Consolidation and basis of presentation The consolidated financial statements include the accounts of MasterCard and its majority-owned and controlled entities, including the Company s variable interest entity. The Company s variable interest entity was established for the purpose of constructing the Company s global technology and operations center; it was not an operating entity and had no employees. In March 2009, the Company discontinued its use of the variable interest entity. See Note 11 (Consolidation of Variable Interest Entity) for further discussion. Intercompany transactions during the periods ended March 31, 2009 and 2008 have been eliminated in consolidation. The Company follows accounting principles generally accepted in the United States of America (GAAP).

The balance sheet as of December 31, 2008 was derived from the audited consolidated financial statements as of December 31, 2008. The consolidated financial statements for the three months ended March 31, 2009 and 2008 and as of March 31, 2009 are unaudited, and in the opinion of management, include all normal recurring adjustments that are necessary to present fairly the results for interim periods. Due to seasonal fluctuations and other factors, the results of operations for the three months ended March 31, 2009 are not necessarily indicative of the results to be expected for the full year.

The accompanying unaudited consolidated financial statements are presented in accordance with the U.S. Securities and Exchange Commission requirements of Quarterly Reports on Form 10-Q and, consequently, do not include all of the disclosures required by GAAP. Reference should be made to the MasterCard Incorporated Annual Report on Form 10-K for the year ended December 31, 2008 for additional disclosures, including a summary of the Company s significant accounting policies.

Reclassification of prior period amounts and recent accounting pronouncements Certain prior period amounts have been reclassified to conform to the 2009 presentation. The amounts reclassified primarily relate to the adoption of certain accounting standards and the reclassification of certain cardholder-related enhancement expenses, which were previously classified as advertising and marketing expenses, to general and administrative expenses. These cardholder benefit program expenses, such as insurance and card replacements, were previously deemed promotional features of the cards and over time have become standard product offerings in certain card categories. Approximately $20,000 of these expenses have been reclassified for the three months ended March 31, 2008 to conform to the 2009 presentation.

With respect to adoption of accounting standards, the provisions of Financial Accounting Standards Board (FASB) Staff Position (FSP) EITF 03-6-1, Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities (FSP EITF 03-6-1) became effective for the Company on January 1, 2009, resulting in the retroactive adjustment of earnings per share (EPS) for prior periods. See Note 2 (Earnings Per Share) for further detail.

In December 2007, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 160, Noncontrolling Interests in Consolidated Financial Statements an amendment of ARB No. 51 (SFAS 160). SFAS 160 amends Accounting Research Bulletin (ARB) No. 51, Consolidated Financial Statements and establishes accounting and reporting standards that require non-controlling interests, previously referred to as minority interests, to be reported as a component of equity. In addition, changes in a parent s ownership interest while the parent retains its controlling interest are accounted for as equity transactions, and upon a gain or loss of control, retained ownership interests are remeasured at fair value, with any gain or loss recognized in earnings. Effective January 1, 2009, the Company applied the provisions of SFAS 160 retrospectively in the consolidated

MASTERCARD INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

(In thousands, except per share and percent data)

financial statements. The adoption of SFAS 160 did not have a material impact on the Company s financial position or results of operations for any periods presented.

The provisions of FASB No. 161, Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133 (SFAS 161) became effective for the Company on January 1, 2009. SFAS 161 applies to all entities and requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of and gains and losses on derivative instruments, and disclosures about credit-risk related contingent features in derivative agreements. The Company applied the requirements of SFAS 161 on a prospective basis. Accordingly, disclosures related to interim periods prior to the date of adoption have not been presented. Since SFAS 161 relates to disclosures only, it had no impact on the Company s financial position or results of operations. See Note 18 (Foreign Exchange Risk Management) for further detail.

Effective January 1, 2009, the Company adopted SFAS No. 141(R), Business Combinations (SFAS 141(R)). SFAS 141(R) establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree; how the acquirer recognizes and measures the goodwill acquired in a business combination; and how the acquirer determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. The adoption of SFAS 141(R) did not have a material impact on the Company s financial position or results of operations as of or for the three months ended March 31, 2009.

In April 2009, the FASB issued FSP No. FAS 107-1 and APB 28-1, Interim Disclosures about Fair Value of Financial Instruments (FSP FAS 107-1 and APB 28-1) which requires public entities to disclose in their interim financial statements the fair value of all financial instruments within the scope of FASB Statement No. 107, *Disclosures about Fair Value of Financial Instruments* , as well as the method(s) and significant assumptions used to estimate the fair value of those financial instruments. The Company will adopt FSP FAS 107-1 and APB 28-1 by making the required additional financial statement disclosures during the second quarter of 2009. The adoption of FSP FAS 107-1 and APB 28-1 will have no financial impact on our consolidated financial statements.

Also in April 2009, the FASB issued FSP No. FAS 115-2 and FAS 124-2, Recognition and Presentation of Other-Than-Temporary Impairments (FSP FAS 115-2 and FAS 124-2) to change the method for determining whether an other-than-temporary impairment exists for debt securities and the amount of an impairment charge to be recorded in earnings. FSP FAS 115-2 and FAS 124-2 also requires enhanced disclosures, including the Company s methodology and key inputs used for determining the amount of credit losses recorded in earnings. The Company will adopt FSP FAS 115-2 and FAS 124-2 during the second quarter of 2009 and is evaluating the impact of the adoption on its consolidated financial statements.

Finally, the FASB issued FSP No. FAS 157-4, Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly (FSP FAS 157-4) during April 2009. FSP FAS 157-4 provides additional guidance to highlight and expand on the factors that should be considered in estimating fair value when there has been a significant decrease in market activity for a financial asset. FSP FAS 157-4 also requires new disclosures relating to fair value measurement inputs and valuation techniques (including changes in inputs and valuation techniques). The Company will adopt FSP FAS 157-4 during the second quarter of 2009 and is evaluating the impact of the adoption on its consolidated financial statements.

Note 2. Earnings Per Share

FSP EITF 03-6-1 became effective January 1, 2009 with retrospective application. Under FSP EITF 03-6-1, unvested share-based payment awards which receive non-forfeitable dividend rights, or dividend equivalents, are considered participating securities and are required to be included in computing earnings per share under the two-class method. The Company declared non-forfeitable dividends on unvested restricted stock units and contingently issuable performance stock units (Unvested Units) which were granted prior to 2009 and therefore has presented EPS under the two-class method pursuant to FSP EITF 03-6-1.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

(In thousands, except per share and percent data)

The components of basic and diluted EPS for common shares under the two-class method for the three months ended March 31 were as follows:

	2009	2008
Numerator:		
Net income attributable to MasterCard	$ 367,258	$ 446,878
Less: Net income allocated to Unvested Units	2,691	3,423
Net income attributable to MasterCard allocated to common shares	$ 364,567	$ 443,455
Denominator:		
Basic EPS weighted average shares outstanding	129,636	131,426
Dilutive stock options and stock units	339	338
Diluted EPS weighted-average shares outstanding	129,975	131,764
Earnings per Share		
Total Basic	$ 2.81	$ 3.37
Total Diluted	$ 2.80	$ 3.37

The calculation of diluted earnings per share excluded approximately 290 and 141 stock options for the three months ended March 31, 2009 and 2008, respectively, because the effect would have been antidilutive.

The following table compares EPS as originally reported and EPS under the two-class method, pursuant to FSP EITF 03-6-1, to quantify the impact of the new standard on EPS for the three months ended March 31, 2008.

Basic as originally reported	$ 3.40
Basic pursuant to FSP EITF 03-6-1	$ 3.37
Impact of FSP EITF 03-6-1 on basic EPS	$ (0.03)
Diluted as originally reported	$ 3.38
Diluted pursuant to FSP EITF 03-6-1	$ 3.37
Impact of FSP EITF 03-6-1 on diluted EPS	$ (0.01)

Note 3. Non-Cash Investing and Financing Activities

The following table includes non-cash investing and financing information for each of the three month periods ended March 31:

	2009	2008
Dividends declared but not yet paid	$ 19,691	$ 19,992
Liabilities assumed related to investments in affiliates	8,750	
Municipal bonds cancelled	154,000 [1]	
Revenue bonds received	(154,000)[2]	
Building and land assets recorded pursuant to capital lease	(154,000)[2]	
Capital lease obligation	154,000 [2]	

1 See Note 11 (Consolidation of Variable Interest Entity) for further details.
2 See Note 7 (Property, Plant, and Equipment) for further details.

Note 4. Fair Value

Certain financial instruments are carried at cost on the consolidated balance sheets, which approximates fair value due to their short-term, highly liquid nature. These instruments include cash and cash equivalents, accounts receivable, settlement due from customers, restricted security deposits held for customers, prepaid expenses, accounts payable, settlement due to customers and accrued expenses.

Pursuant to the provisions of SFAS No. 157, Fair Value Measurements (SFAS 157), which the Company adopted effective January 1, 2008, the Company classifies its fair value measurements in a three-level hierarchy (the

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MASTERCARD INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

(In thousands, except per share and percent data)

Valuation Hierarchy). The distribution of the Company s financial instruments, which are measured at fair value on a recurring basis, within the Valuation Hierarchy, is as follows:

	Quoted Prices in Active Markets (Level 1)		Significant Other Observable Inputs (Level 2)		Significant Unobservable Inputs (Level 3)		Fair Value at March 31, 2009
Municipal bonds[1]	$		$ 493,294	$		$	493,294
Taxable short-term bond funds		104,313					104,313
Auction rate securities					191,240		191,240
Foreign currency forward contracts			27,669				27,669
Other		62					62
Total	$	104,375	$ 520,963	$	191,240	$	816,578

	Quoted Prices in Active Markets (Level 1)		Significant Other Observable Inputs (Level 2)		Significant Unobservable Inputs (Level 3)		Fair Value at December 31, 2008
Municipal bonds[1]	$		$ 485,490	$		$	485,490
Taxable short-term bond funds		102,588					102,588
Auction rate securities					191,760		191,760
Foreign currency forward contracts			33,731				33,731
Other		17					17
Total	$	102,605	$ 519,221	$	191,760	$	813,586

1 Available-for-sale municipal bonds are carried at fair value and are included in the above tables. However, held-to-maturity municipal bonds are carried at amortized cost and excluded from the above tables.

The Company holds investments in auction rate securities (ARS). Interest on these securities is exempt from U.S. federal income tax and the interest rate on the securities typically resets every 35 days. The securities are fully collateralized by student loans with guarantees, ranging from approximately 95% to 98% of principal and interest, by the U.S. government via the Department of Education.

Beginning on February 11, 2008, the auction mechanism that normally provided liquidity to the ARS investments began to fail. Since mid-February 2008, all 44 investment positions in the Company s ARS investment portfolio have experienced failed auctions. The securities for which auctions have failed have continued to pay interest in accordance with the contractual terms of such instruments and will continue to accrue interest and be auctioned at each respective reset date until the auction succeeds, the issuer redeems the securities or they mature. As of March 31, 2009, the ARS market remained illiquid but issuer call and redemption activity in the ARS student loan sector has occurred periodically since the auctions began to fail. During the three months ended March 31, 2009, the Company did not sell any ARS but there were some partial calls of ARS.

The Company continues to believe that the fair value of its ARS portfolio does not approximate par value due to the continued lack of liquidity in the ARS market. The Company has considered the continued lack of liquidity in the ARS market and the lack of comparable, orderly transactions when estimating the fair value of its ARS portfolio. Due to the lack of comparable, orderly transactions and pursuant to the provisions of SFAS 157, the Company utilized the income approach, which included a discounted cash flow analysis of the estimated future cash flows for the ARS portfolio as of March 31, 2009, to estimate the fair value of its ARS portfolio. Based on this approach, the Company estimated a 20% discount to the par value of the ARS portfolio. The temporary impairment included in accumulated other comprehensive income related to the Company s ARS was $47,810 and $47,940 as of March 31, 2009 and December 31, 2008, respectively. A hypothetical increase of 100 basis points in the discount rate used in the discounted cash flow analysis would have increased the temporary impairment by approximately $24,000 at each period end.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

(In thousands, except per share and percent data)

The Company evaluated the estimated impairment of its ARS portfolio to determine if it was other-than-temporary. The Company considered several factors including, but not limited to, the following: (1) the reasons for the decline in value (credit event, interest related or market fluctuations); (2) MasterCard s ability and intent to hold the investments for a sufficient period of time to allow for recovery of value; (3) whether the decline is substantial; and (4) the historical and anticipated duration of the events causing the decline in value. The evaluation for other-than-temporary impairments is a quantitative and qualitative process, which is subject to various risks and uncertainties. The risks and uncertainties include changes in the credit quality of the securities, changes in liquidity affected by the auction mechanism or issuer calls of the securities and the effects of changes in interest rates. As of March 31, 2009, the Company had the ability and intent to hold its ARS investments until recovery of fair value, which may be maturity or earlier if called, and therefore did not consider unrealized losses to be other-than-temporary.

The ARS investments have been classified within level 3 of the Valuation Hierarchy as their valuation requires substantial judgment and estimation of factors that are not currently observable in the market due to the lack of trading in the securities. This valuation may be revised in future periods as market conditions evolve.

The table below includes a roll-forward of the Company s ARS investments from January 1, 2009 to March 31, 2009. When a determination is made to classify a financial instrument within level 3, the determination is based upon the significance of the unobservable parameters to the overall fair value measurement. However, the fair value determination for level 3 financial instruments may include observable components.

	Significant Unobservable Inputs (Level 3)
Fair value, January 1, 2009	$ 191,760
Calls, at par	(650)
Recovery of unrealized losses due to issuer calls[1]	130
Fair value, March 31, 2009	$ 191,240

[1] Unrealized gains and losses on available-for-sale securities are recorded as a separate component of other comprehensive income on the consolidated statements of comprehensive income. Due to issuer calls at par value during the three months ended March 31, 2009, certain unrealized losses recorded in prior periods were recovered and removed from other comprehensive income.

The table below summarizes the maturity ranges of the ARS portfolio, based on relative par value, as of March 31, 2009:

	Par Amount	**% of Total**
Due within 10 years	$ 4,000	2%
Due year 11 through year 20	42,100	17%
Due year 21 through year 30	141,200	59%
Due after year 30	51,750	22%
Total	$ 239,050	100%

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MASTERCARD INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

(In thousands, except per share and percent data)

In accordance with FASB Staff Position FAS 157-2, Effective Date of FASB Statement No. 157 (FSP SFAS 157-2), the provisions of SFAS 157 became effective for the Company s nonfinancial assets and nonfinancial liabilities that are measured at fair value on a nonrecurring basis on January 1, 2009. The Company s nonfinancial assets for which the provisions of SFAS 157 are now effective include property, plant and equipment, goodwill and other intangible assets. The impact of applying the provisions of SFAS 157 to the Company s nonfinancial assets was not material.

The valuation methods for goodwill and other intangibles involve assumptions concerning interest and discount rates, growth projections and other assumptions of future business conditions. The assumptions employed are based on management s judgment using internal and external data and as such, fair value determinations related to goodwill and other intangible assets are classified in level 3 of the Valuation Hierarchy.

Note 5. Prepaid Expenses

Prepaid expenses consisted of the following:

	March 31, 2009	December 31, 2008
Customer and merchant incentives	$ 420,010	$ 397,563
Advertising	50,668	45,608
Data processing	30,063	24,455
Other	22,212	48,081
Total prepaid expenses	522,953	515,707
Prepaid expenses, current	(206,572)	(213,612)
Prepaid expenses, long-term	$ 316,381	$ 302,095