Exit Strategies for Government Contractors
Public Pricing Trends

PUBLIC PRICING FROM 1/2/08 TO 8/31/11

- Obama Elected
- FY 2010 Budget Proposal
- Gates DoD Budget Cut Proposal
- LehmanCollapse
- FY 2009 Budget Proposal
- Market Trough
- FY 2011 Budget Proposal
- FY 2012 Budget Proposal
- Mid-Term Elections
- Debt Deal / S&P Downgrade
- 8/31/2011

S&P 500 (8.6%)
G (9.8%)
Primes (27.1%)

Government Services: BAH, CACI, DRCO, ICFI, KEYW, KTOS, LSE:QQ, MANT, NCIT, and SAI
Prime Contractors: BA, GD, ITT, LLL, LMT, LSE:BA, NOC, and RTN
Source: Capital IQ
Public Company Valuation Trends

**Enterprise Value / LTM Revenue**

**Government Services**
- BAH, CACI, DRCO, ICFI, KTOS, LSE:QQ, MANT, NCIT, SAI, and SRX

**Prime Contractors**
- BA, GD, ITT, LLL, LMT, LSE:BA, NOC, and RTN

Source: Capital IQ

**Enterprise Value / LTM EBITDA**

**Government Services**
- BAH, CACI, DRCO, ICFI, KTOS, LSE:QQ, MANT, NCIT, SAI, and SRX

**Prime Contractors**
- BA, GD, ITT, LLL, LMT, LSE:BA, NOC, and RTN

Source: Capital IQ
M&A Valuation Trends

Government Services M&A Valuation Trends

Government Services: BAH, CACI, DRCO, ICFI, KTOS, LSE:QQ, MANT, NCIT, SAI, and SRX
Source: Capital IQ, Washington Technology, KippsDeSanto research
2011 YTD through 8/31/11

Transaction Volume | Median Transaction Multiple | Public Gov't Services Multiple

2004: 106 | 8.8x | 14.8x
2005: 100 | 9.9x | 10.9x
2006: 84 | 10.1x | 10.3x
2007: 99 | 10.6x | 10.7x
2008: 91 | 8.4x | 10.2x
2009: 77 | 9.2x | 10.7x
2010: 99 | 8.2x | 9.3x
2011 YTD: 52 | 7.3x | 10.7x

Source: Capital IQ, Washington Technology, KippsDeSanto research
2011 YTD through 8/31/11
M&A Transaction Volume Breakdown

**Transactions by Target Customer**

- Intel / Cyber: 35%
- Diversified: 21%
- Civilian: 28%
- DoD: 16%

(1) Reflects analysis of 228 Government Services M&A transactions from January 1, 2009 – August 31, 2011
Source: Washington Technology, KippsDeSanto research and estimates

**Transaction Size**

- Greater than $100M: 21%
- $25M-$100M: 29%
- Less than $25M: 50%

(1) Reflects analysis of 228 Government Services M&A transactions from January 1, 2009 – August 31, 2011
Source: Washington Technology, KippsDeSanto research and estimates
Buyer Universe

**Government Services Transactions by Buyer Type**

- **Gov't Services - Public**: 23%
- **Gov't Services - Private**: 17%
- **Gov't Services - PEG Backed**: 14%
- **Commercial**: 17%
- **Private Equity**: 12%
- **Foreign**: 7%
- **Aerospace / Defense**: 10%
- **Private**: 17%
- **Foreign**: 7%

Reflects analysis of 228 Government Services M&A transactions from January 1, 2009 – August 31, 2011

Source: Washington Technology, KippsDeSanto research
Drivers of Value

**GROWTH**
- Double-digit historical and projected growth
- Growing focus sectors
- Flat or declining revenue

**RISK**
- F&O contract base
- Long-term contracts / task orders
  - Set-aside contract dependency
  - Lower margins

**LEVERAGABILITY**
- Large, transitionable contract vehicles
- Sought-after customers
- Unique capabilities
- Lack of focus / depth
Deals That Get Done

**FOCUS**
- Growing, Priority Market
- Attractive Customer Base
- Direct Mission Support

**DEPTH**
- Go-to Contractor for Key Customers
- Excellence in Select Core Capabilities as Opposed to Diversified Services Providers

**INTELLECTUAL PROPERTY**
- Technology
- Tools
- Processes

**IDENTITY**
- Clear Distinction: Performer or Advisor
- “Known” Quantity with Customers

---

SEIA
Signature Equity & Investment Advisors, LLC
www.SEIA.com

WATKINS | MEEGAN

KippsDeSanto
INVESTMENT BANKING
# Scorecard of M&A Attractiveness

<table>
<thead>
<tr>
<th>Metric</th>
<th>Company X</th>
<th>Threshold</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>Size</td>
<td>2011E Rev.: $110 Million</td>
<td>$100+ Million for Most Aggressive Buyers</td>
<td>+</td>
</tr>
<tr>
<td>Set-aside Exposure</td>
<td>&lt; 10% of Revenue</td>
<td>&lt; 20% of Revenue</td>
<td>+</td>
</tr>
<tr>
<td>Profitability</td>
<td>8 to 10% Adjusted EBITDA Margin</td>
<td>8% to 10% EBITDA Margins</td>
<td>+</td>
</tr>
<tr>
<td>Growth</td>
<td>10.7% CAGR 2009 – 2011E</td>
<td>10% to 15% Annual Growth</td>
<td>+</td>
</tr>
<tr>
<td>Prime / Sub Mix</td>
<td>2011E: 50% Prime; 50% Sub</td>
<td>Prime Position is Highly Favored</td>
<td>-</td>
</tr>
<tr>
<td>Customers</td>
<td>Air Force, USMC, Fed-Civil</td>
<td>2-4 Core Customers; Domain Expertise</td>
<td>+</td>
</tr>
<tr>
<td>Capabilities</td>
<td>Cybersecurity, Network Operations, Health IT, Cloud Computing</td>
<td>Highly Coveted / Focused</td>
<td>+</td>
</tr>
</tbody>
</table>
# Sample Strategic Alternatives

## Internal

<table>
<thead>
<tr>
<th>Considerations</th>
<th>Status Quo</th>
<th>Acquisition Strategy</th>
<th>ESOP Recap</th>
<th>Non-ESOP Leveraged Recap</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mgmt. / Employee Control / Sustain Legacy</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Improved Company Opportunities / Posture</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Transformation / Integration Risk</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Transaction Feasibility</td>
<td>NA</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Value Proposition</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investment Risk</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Liquidity</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tax Advantages</td>
<td>NA</td>
<td>NA</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

## External

<table>
<thead>
<tr>
<th>Considerations</th>
<th>Minority Sale</th>
<th>IPO</th>
<th>Sale to Financial Buyer</th>
<th>Sale to Strategic Buyer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mgmt. / Employee Control / Sustain Legacy</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Improved Company Opportunities / Posture</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Transformation / Integration Risk</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Transaction Feasibility</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Value Proposition</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investment Risk</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Liquidity</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tax Advantages</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Transaction Timing Determinants

**Shareholder Considerations**
- Liquidity desires
- Valuation requirements
- Professional / personal aspirations

**Capital / M&A Market Conditions**
- Peer group valuations
- Breadth of buyer universe and level of acquisition interest
- Competitiveness for volume of deals in-market
- Availability of capital

**Business Performance**
- Full and Open revenue and profit visibility and momentum
- Positioning in priority markets
- Strength of customer relationships
- Contract backlog / profile

**Industry / Competitive Trends**
- Budget trends
- Political and regulatory landscape
- Contracting environment (e.g., bundling, protests)

**Management Team**
- Strength and depth of leadership
- Professional / personal aspirations
- Quality of infrastructure
Sample Process Alternatives

**PROCESS A: PRE-EMPTIVE / NARROW APPROACH**

- Contact select strategic buyers that have already expressed interest in similar companies / capabilities / markets
- Focus energy on developing data room and management presentation
- Provide data package and instruction letter for indications
- Negotiate aggressively to get terms at or above valuation expectations and market norms

**PROS / CONS**

▲ Ability to customize the story for each buyer
▲ Speed (potentially)
▲ Less disruptive to management
▲ Easier to shut down if values do not meet expectations
▲ Efficient process
▼ Uncertain if process achieved highest value and best terms
▼ Difficult to communicate full story
▼ Potentially fewer bids from which to choose
▼ Early fall out could make it difficult to create a competitive environment

**PROCESS B: TARGETED APPROACH**

- Contact broader targeted universe of strategic and financial buyers
- Structure process with multiple decision points to enhance competition
- Draft comprehensive CIM
- Full data room
- Conduct 6 to 10 management visits

**PROS / CONS**

▲ Highest confidence in maximizing value
▲ Easier to communicate full strategy / business opportunities
▲ Higher likelihood of capturing pro forma or run rate projections, if applicable
▲ Higher likelihood of hyper-competitive bidding
▲ Broad processes work
▼ Slower process – longer time to close (potentially)
▼ Requires more management time and resources
▼ Risk of tainting the business if chose not to sell
▼ Harder to customize story for best buyers
▼ Requires greater oversight to maintain confidentiality
# Sale Process Components

- A targeted sale process typically requires approximately 5 - 6 months to complete

## Preparation (~3-6 weeks)
- Conduct due diligence
- Develop marketing strategy and buyer list
- Prepare CIM / financial model
- Prepare confidentiality agreements ("CA")
- Finalize marketing materials

## Marketing (~6 weeks)
- Qualify and contact approved buyers
- Approach potential lenders to get early debt feedback
- Distribute CIM subject to signed CA
- Prepare management presentations / begin construction of virtual data room
- Solicit initial indications / select buyers participating in management briefings

## Due Diligence (~5 weeks)
- Conduct company visits / management presentations
- Support buyer preliminary due diligence with opening of data room
- Distribute draft of purchase agreement (if appropriate)
- Solicit final offers / select preferred buyer

## Finalize Transaction (~6 weeks)
- Negotiate and execute definitive agreement
- Conduct final due diligence
- Submit regulatory filing (if necessary)
- Close transaction
Role of Investment Banker

- Bankers advise, resolve issues, coach, facilitate, and negotiate to create actionable alternatives for their clients

Critical Junctures in the “Front-End” Process

- Determining shareholder and management objectives
- Developing the appropriate sale strategy / process
- Identifying timing to initiate a process
- Crafting the appropriate sale document
- Conveying the “story” and opportunities
- Identifying the best strategic and financial buyers
- Deciphering initial indications
- Assembling a competitive group of visitors
- Showcasing the Company and management to visitors

Critical Junctures in the “Back-End” Process

- Fully understanding all final proposals to develop a “true” comparison between bids
- Establishing the right next steps
- Determining the most advantageous time to negotiate with potential buyers
- Developing counter proposal(s) and the best script with which to deliver them
- Craft a process to maintain leverage through closing
- Drive all parties to move expeditiously through closing
## Build a Relationship to Enhance Value

<table>
<thead>
<tr>
<th><strong>SEPTEMBER 2011</strong></th>
<th><strong>DECEMBER 2011</strong></th>
<th><strong>MARCH 2012</strong></th>
<th><strong>JUNE 2012</strong></th>
<th><strong>OCTOBER 2012</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Market update</td>
<td>Market update</td>
<td>Market update</td>
<td>Market update</td>
<td>Market update</td>
</tr>
<tr>
<td>Key ways to create value and roadmap to business and operational transformation</td>
<td>Key ways to create value and roadmap to business and operational transformation</td>
<td>Key ways to create value and roadmap to business and operational transformation</td>
<td>Key ways to create value and roadmap to business and operational transformation</td>
<td>Key ways to create value and roadmap to business and operational transformation</td>
</tr>
<tr>
<td>Market update</td>
<td>Market update</td>
<td>Market update</td>
<td>Market update</td>
<td>Market update</td>
</tr>
<tr>
<td>Tax and estate planning</td>
<td>Tax and estate planning</td>
<td>Tax and estate planning</td>
<td>Tax and estate planning</td>
<td>Tax and estate planning</td>
</tr>
<tr>
<td>Maintaining a strong balance sheet and industry level net working capital</td>
<td>Maintaining a strong balance sheet and industry level net working capital</td>
<td>Maintaining a strong balance sheet and industry level net working capital</td>
<td>Maintaining a strong balance sheet and industry level net working capital</td>
<td>Maintaining a strong balance sheet and industry level net working capital</td>
</tr>
<tr>
<td>Awareness and involvement in key industry events, developing public image, and achieving high visibility awards</td>
<td>Awareness and involvement in key industry events, developing public image, and achieving high visibility awards</td>
<td>Awareness and involvement in key industry events, developing public image, and achieving high visibility awards</td>
<td>Awareness and involvement in key industry events, developing public image, and achieving high visibility awards</td>
<td>Awareness and involvement in key industry events, developing public image, and achieving high visibility awards</td>
</tr>
<tr>
<td>Market update</td>
<td>Market update</td>
<td>Market update</td>
<td>Market update</td>
<td>Market update</td>
</tr>
<tr>
<td>Waterfall preparation</td>
<td>Waterfall preparation</td>
<td>Waterfall preparation</td>
<td>Waterfall preparation</td>
<td>Waterfall preparation</td>
</tr>
<tr>
<td>Maintaining accessible and digitized corporate books and records</td>
<td>Maintaining accessible and digitized corporate books and records</td>
<td>Maintaining accessible and digitized corporate books and records</td>
<td>Maintaining accessible and digitized corporate books and records</td>
<td>Maintaining accessible and digitized corporate books and records</td>
</tr>
<tr>
<td>Finalize advisor team</td>
<td>Finalize advisor team</td>
<td>Finalize advisor team</td>
<td>Finalize advisor team</td>
<td>Finalize advisor team</td>
</tr>
<tr>
<td>Identify objectives and set path for 2013 deal closing</td>
<td>Identify objectives and set path for 2013 deal closing</td>
<td>Identify objectives and set path for 2013 deal closing</td>
<td>Identify objectives and set path for 2013 deal closing</td>
<td>Identify objectives and set path for 2013 deal closing</td>
</tr>
</tbody>
</table>
Posture with Interested Parties

• The optimal approach is for the company to remain “behind the curtain” until the sale process is underway and the appropriate group of potential buyers are contacted in a coordinated marketing effort
  – Don’t maintain a “revolving door” policy with buyers
Intersection of Business & Personal Wealth

**BUSINESS**
- Retirement Plans
- Cash Management
- Executive Benefits
- Business Succession
- Key Employee Retention
- Tax Planning

**SEIA**

Unlock the equity and realize the value of your business with exit planning strategies.

**PERSONAL**
- Retirement Planning
- Investment Management
- Cash Flow Planning
- Estate Planning
- Charitable Planning
- Insurance Portfolio
Exit Strategies

**PRE-SALE**
- Retirement Planning
- Contingency Planning
- Transfer of Stock
- Initial Estate Planning
- Tax Planning

**POST-SALE**
- Investment Management
- Cash Flow Planning
- Advanced Estate Planning
- Charitable Planning
## Exit Strategies through 2012

### 2010 TAX ACT – GIFT TAX

<table>
<thead>
<tr>
<th>Amount Exempt From Gift Tax</th>
<th>2009</th>
<th>2010</th>
<th>2011 &amp; 2012</th>
<th>2013+</th>
</tr>
</thead>
<tbody>
<tr>
<td>$1M</td>
<td>$1M</td>
<td>$5M</td>
<td>$1M</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Gift Tax Rate</th>
<th>2009</th>
<th>2010</th>
<th>2011 &amp; 2012</th>
<th>2013+</th>
</tr>
</thead>
<tbody>
<tr>
<td>45%</td>
<td>35%</td>
<td>35%</td>
<td>55%</td>
<td></td>
</tr>
</tbody>
</table>
## Exit Strategies through 2012

### 2010 TAX ACT – ESTATE & GST TAX

<table>
<thead>
<tr>
<th></th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2013+</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Amount Exempt from</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Estate Tax</strong></td>
<td>$3.5M</td>
<td>100%</td>
<td>$5M</td>
<td>$1M</td>
</tr>
<tr>
<td><strong>Estate/GST Tax Rate</strong></td>
<td>45%</td>
<td>0%</td>
<td>35%</td>
<td>55%</td>
</tr>
</tbody>
</table>
Exit Strategies Timeline

- Retirement Planning
- Contingency Planning
- Initial Estate Planning
- Executive Benefits
- Transfer Of Stock
- Tax Planning
- Sale of Business
- Investment Planning
- Cash Flow Planning
- Advanced Estate Planning
- Charitable Planning
QUALIFIED PLANS

- 401(k)
- Profit Sharing Plan
- Combination Defined Benefit Plans
Executive Benefits

NON-QUALIFIED PLANS

• Deferred Compensation
  – Supplemental Executive Retirement Plan
  – Employee Stock Ownership Plan

• Unfunded
  – Phantom Stock
  – Restricted Stock
  – Stock Appreciation Rights
Ensure that your spouse/family receives FMV for the business in the event of death

• Key Man and Buy/Sell Plans
  – Funded with Term or Permanent Life Insurance

• Ownership options
  – Company, Irrevocable Life Insurance Trust, Cross Purchase Agreements
  – Creative strategy for funding non-qualified executive benefits
Techniques for using unified credit exemption $5M/$10M before 2013

• Intentionally Defective Grantor Trust
• Family Limited Partnerships
• Employee Stock Ownership Plans
**Benefits** of using unified credit exemption

$5M/$10M before 2013

- Minority discounting up to 35%
- Gets future growth of stock out of estate
- Reduces size of estate when sale transaction is complete
- Creates non-voting shares to handle control issues
- Works for companies wishing to transfer some or all of company to a family member who works in the business
- Transfer $10M+ of wealth tax free plus future growth of those assets
Initial Estate Planning

- Revocable Trust
- Irrevocable Trusts
  - Dynasty
  - Irrevocable Life Insurance Trust
  - Grantor Retained Annuity Trust
- Insurance to cover:
  - Family liabilities
  - Taxes
  - Insure that your family receives FMV of business
Tax Planning

- Get your tax / accounting advisor involved early on
- Understand the tax implications of different entity types and what IRS rules apply
- Asset sale or stock sale, know the difference
- What is goodwill, how is it calculated?
- Ordinary Income Rates vs. Capital Gains Rates, what goes where?
- How Earn Out affects taxes paid, timing, etc.
Cash Flow Planning

“Four Horseman” Financial Planning Scenarios:

- High taxes
- Inflation
- Monte Carlo
- Black Swan
Create a portfolio with portion of sale proceeds:

- Create/review Investment Policy Statement
- Monte Carlo simulation
- Tax considerations
- Alternative investment considerations
Create liquidity in entity outside your estate to:

- Reduce potential estate taxes
- Maximize wealth to heirs and charitable interests
Advanced Estate Planning

Techniques:

• Annual gifting
• Lifetime gifting
• Grantor Retained Annuity Trust with marketable securities
• Family Limited Partnership for Real Estate LLC
• Insurance Strategies
Charitable Planning

Techniques:
• Charitable Remainder Trust
• Foundations
• Charitable Lead Trust
Exit Strategies Timeline

Managing These Problems:

It’s Not Easy
Building Your Team

Wealth Management

Finance

Accounting

Legal