Science Applications International Corp
Form 10-K
March 29, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

(Mark One)

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended January 29, 2016

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	Exact Name of Registrant as Specified in its Charter, Address of Principal Executive Offices and Telephone Number	State or other jurisdiction of incorporation or organization	I.R.S. Employer Identification No.
001-35832	Science Applications International Corporation 1710 SAIC Drive, McLean, Virginia 22102 703-676-4300	Delaware	46-1932921

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Science Applications International Corporation	New York Stock Exchange

Common Stock, Par Value $.0001 Per Share

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.	Yes x	No ¨
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.	Yes ¨	No x
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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).	Yes x	No ¨
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.	x	

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.

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company ¨

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

As of July 31, 2015 (the last business day of the registrant's most recently completed second quarter), the aggregate market value of the registrant's common stock (based upon the closing stock price) held by non-affiliates was $2.3 billion.

The number of shares issued and outstanding of the registrant's common stock as of March 4, 2016 was 44,775,496 shares ($.0001 par value per share).

DOCUMENTS INCORPORATED BY REFERENCE

Portions of Science Applications International Corporation's Definitive Proxy Statement for the 2016 Annual Meeting of Stockholders are incorporated by reference in Part III of this report.

SCIENCE APPLICATIONS INTERNATIONAL CORPORATION

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Part I

Item 1. Business

The Company

Science Applications International Corporation (herein referred to as “SAIC,” the “Company,” “we,” “us,” or “our”) is a leadin provider of technical, engineering and enterprise information technology (IT) services primarily to the U.S. government, including the Department of Defense (DoD), the intelligence community and federal civilian agencies. We provide engineering, systems integration and information technology offerings for large, complex government projects and offer a broad range of services with a targeted emphasis on higher-end, differentiated technology services. Our end-to-end enterprise IT offerings span the entire spectrum of our customers’ IT infrastructure. We commenced operations on September 27, 2013 (the Distribution Date) following completion of a spin-off transaction from our former parent, Leidos Holdings, Inc. (collectively with its consolidated subsidiaries, “former Parent”).

Our business has a long and successful history, tracing its roots to the earliest days of former Parent which was founded in 1969 as a scientific research and engineering firm. Our customers include all branches of the U.S. military (Army, Air Force, Navy, Marines and Coast Guard), U.S. Defense Logistics Agency, National Aeronautics and Space Administration (NASA), U.S. Department of State, and U.S. Department of Homeland Security (DHS). In May 2015 we completed the acquisition of privately held Scitor Holdings, Inc. (Scitor), a leading provider of services to the intelligence community, which enables us to gain access to new customers primarily in the classified workspace. Our long-standing customer relationships have enabled us to achieve an in-depth understanding of our customers’ missions and provide differentiated service offerings to meet our customers’ most complex requirements. Our offerings include: engineering; technology and equipment platform integration; maintenance of ground and maritime systems; logistics; training and simulation; operation and program support services; and end-to-end services spanning the design, development, integration, deployment, management and operations, sustainment and security of our customers’ entire IT infrastructure. We serve our customers through approximately 1,700 active contracts and task orders. We have approximately 15,000 employees that are led by an experienced executive team of proven industry leaders.

Our core strengths have supported our successful performance on programs of national importance. Those strengths include:

Enduring Customer Relationships and Mission-Orientation. We have strong and long-lasting relationships with diverse customers throughout the U.S. government. Our track record of serving the missions of our government customers spans decades, including several enduring customer relationships that have lasted 20 years or more. Our employees, many of whom are deployed at customer sites, work closely with our customers in fulfilling their missions. Our strong customer relationships enable us to develop deep customer knowledge and translate our mission understanding into successful program execution that fosters continued demand for our services.

Full Life Cycle Offerings. We integrate technologies and deliver services that provide our customers with seamless end-to-end solutions. Our expertise includes initial requirements definition, development and integration services, training, logistics and sustainment. These full life cycle offerings, combined with deep customer knowledge, allow us to more effectively support our customers’ missions.

Significant Scale and Diversified Contract Base. With approximately $4.3 billion in revenue in fiscal 2016, we are one of the largest pure play technical service providers to the U.S. government. Our significant scale advantage enables us to serve as prime systems integrator on large, complex programs and to allocate resources toward further developing and expanding our repeatable, proven solutions and differentiated technical capabilities. Our diversified revenue base consists of programs ranging from research and development to operations and maintenance.

Technical Experts Led by Experienced Management. The quality, training and knowledge of our employees are important competitive assets. Our skilled workforce ranges from entry-level technicians to expert-level professionals in network engineering, software design and development, logistics, technology integration and systems engineering. Additionally, the majority of our workforce holds an active security clearance, which is required on many of our existing programs and future program opportunities.

SCIENCE APPLICATIONS INTERNATIONAL CORPORATION

Our workforce is led by a talented and experienced senior leadership team with a long history of solving our customers’ most difficult challenges. Collectively, our executive team averages more than 25 years of industry experience, consisting of members who have served as senior leaders in public companies and are recognized as leaders in their respective markets by customers and partners.

Repeatable Methodologies and Certified Processes. Our technical excellence is driven by our proven, repeatable, disciplined processes for management, engineering, technical support and services. We deploy our tools and processes enterprise-wide and emphasize a consistent approach to planning, designing, and delivering solutions and services to our customers. We hold certifications from the International Organization for Standardization (including ISO 9001:2008, ISO/IEC 27001:2013, ISO 20000-1:2011 and AS9100), and from the Capability Maturity Model Integration Institute as a CMMI®-DEV Maturity Level 3 organization.

Each of our operating segments is focused on providing our full range of offerings to its respective customer base. Our operating segments have been aggregated into one reportable segment for financial reporting purposes.

For additional discussion and analysis related to recent business developments, see “Economic Opportunities, Challenges and Risks” in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Part II of this report.

Key Customers

In each of fiscal 2016, 2015 and 2014, over 95% of our total revenues were attributable to prime contracts with the U.S. government or to subcontracts with other contractors engaged in work for the U.S. government. Substantially all of our revenues were earned by entities located in the United States.

We generated more than 10% of our total revenues during each of the last three fiscal years from each of the U.S. Army and U.S. Navy. The percentages of total revenues for the U.S. government, its agencies and other customers, including those comprising more than 10% of total revenues for each of the three years ended January 29, 2016 were:

	Year Ended January 29, 2016		January 30, 2015		January 31, 2014	
U.S. Army	29	%	28	%	29	%
U.S. Navy	16	%	20	%	21	%
Other DoD	21	%	22	%	22	%
Other federal government	31	%	27	%	25	%
Total U.S. government	97	%	97	%	97	%
Other	3	%	3	%	3	%
Total	100	%	100	%	100	%

The U.S. Army and the U.S. Navy have a number of subordinate agencies, which have separate budgets and procurement functions. Our contracts may be with the highest level of these agencies, with the subordinate agencies of these customers or as a subcontractor to other contractors engaged in work for the same.

Regulation

Our business is heavily regulated and we must comply with and are affected by laws and regulations relating to the award, administration and performance of U.S. government and other contracts. U.S. government contracts generally are subject to the Federal Acquisition Regulation (FAR), which sets forth policies, procedures and requirements for the acquisition of goods and services by the U.S. government. We may also be subject to agency-specific regulations that supplement the FAR (such as the DoD's Defense Federal Acquisition Regulation Supplement) as well as other applicable laws and regulations. These regulations impose a broad range of requirements, many of which are unique to government contracting and include procurement, import and export, security, contract termination and adjustment, and audit requirements. In addition, these regulations govern contract pricing and reimbursable costs by, among other things, requiring certification and disclosure of cost or pricing data in connection with certain contract negotiations, defining allowable and unallowable costs, and otherwise governing the right to reimbursement under various flexibly priced contracts. These laws and regulations impose specific cost accounting practices that may increase accounting and internal control costs associated with compliance with government standards.

The U.S. government has the ability to cancel contracts at any time through a termination for the convenience of the U.S. government. Most of our contracts have cancellation terms that would permit us to recover all or a portion of our incurred costs and contract profit for work performed when the U.S. government issues a termination for convenience.

The U.S. government may revise its procurement practices or adopt new contract rules and regulations at any time.

Some of our operations and service offerings involve our access to and use of personally identifiable information and protected health information, which activities are regulated by extensive federal and state privacy and data security laws requiring organizations to provide certain privacy protections and security safeguards for such information.

Internationally, we are subject to foreign government laws and regulations, and U.S. government laws, regulations, and procurement policies and practices (including laws and regulations relating to bribery of foreign government officials, import and export control, investments, exchange controls and repatriation of earnings). We are also susceptible to varying political and economic risks.

In order to help ensure compliance with these complex laws and regulations, we have established policies and procedures that address our approach to meeting these requirements and also administer a robust ethics and compliance training program to maintain a compliance-oriented workforce.

These regulations and risks affecting our business are described in more detail under “Risk Factors” in this report.

Contracts

We must comply with and are affected by laws and regulations relating to the formation, administration and performance of U.S. government and other contracts. The U.S. government procurement environment has evolved due to statutory and regulatory procurement reform initiatives. Budgetary pressures and reforms in the procurement process have increasingly caused many U.S. government customers to purchase services and solutions using contracting processes that give them the ability to select multiple winners or pre-qualify certain contractors to provide various services or solutions on established general terms and conditions rather than through single award contracts. The predominant contracting methods through which U.S. government agencies procure services and solutions include the following:

Single Award Contracts. U.S. government agencies may procure services and solutions through single award contracts which specify the scope of work that will be delivered and identify the contractor that will provide the specified services. When an agency has a requirement, interested contractors are solicited, qualified and then provided with a request for proposal. The process of qualifying prospective bidders, soliciting proposals and evaluating contractor bids requires the agency to maintain a large, professional procurement staff and the bidding and selection process can take a year or more to complete. This method of contracting may provide the contractor with greater certainty of the timing and amounts to be received at the time of contract award because it generally results in the customer contracting for a specific scope of work from the single successful awardee.

Indefinite Delivery, Indefinite Quantity (IDIQ) Contracts. The U.S. government uses IDIQ contracts to obtain commitments from contractors to provide certain services or solutions on pre-established terms and conditions. The U.S. government then issues task orders under the IDIQ contracts to purchase the specific services or solutions it needs. IDIQ contracts are awarded to one or more contractors following a competitive procurement process. Under a single award IDIQ contract, all task orders under that contract are awarded to one pre-selected contractor. Under a multi-award IDIQ contract, task orders can be awarded to any of the pre-selected contractors, which can result in further limited competition for the award of task orders. Multi-award IDIQ contracts that are open for any government agency to use for the procurement of services are commonly referred to as "government-wide acquisition contracts." IDIQ contracts often have multi-year terms and unfunded ceiling amounts that enable, but not commit, the U.S. government to purchase substantial amounts of services or solutions from one or more contractors. At the time an IDIQ contract is awarded (prior to the letting of any task orders), a contractor may have limited or no visibility as to the ultimate amount of services or solutions that the U.S. government will purchase under the contract, and, in the case of a multi-award IDIQ, the contractor from which such purchases may be made.

U.S. General Services Administration (GSA) Schedule Contracts. The GSA maintains listings of approved suppliers of services and solutions with pre-negotiated prices for use throughout the U.S. government. In order for a company to provide services under a GSA Schedule contract, a company must be pre-qualified and awarded a contract by the GSA. When an agency uses a GSA Schedule to meet its requirements, the agency (or the GSA on behalf of the agency) conducts the procurement and bidders are limited to GSA Schedule-qualified contractors. GSA Schedule contracts are designed to provide the user agency with reduced procurement time and lower procurement costs. Similar to IDIQ contracts, at the time a GSA Schedule contract is awarded, a contractor may have limited or no visibility as to the ultimate amount of services or solutions that customers will ultimately purchase under the contract.

Contract Types

Generally, the type of contract used for the acquisition of our services and solutions is determined by or negotiated with the U.S. government and may depend on certain factors, including: the type and complexity of the work to be performed; degree and timing of the responsibility to be assumed by the contractor for the costs of performance; the extent of price competition; and the amount and nature of the profit incentive offered to the contractor for achieving or exceeding specified standards or goals. We generate revenues under several types of contracts, including the following:

- Cost-reimbursement contracts provide for reimbursement of our direct contract costs and allocable indirect costs, plus a fee (contract profit). This type of contract is generally used when uncertainties involved in contract performance do not permit costs to be estimated with sufficient accuracy to use a fixed-price contract. Cost-reimbursement contracts usually subject us to lower risk and generally require us to use our best efforts to accomplish the scope of the work within a specified time and amount of costs.
- Time-and-materials (T&M) contracts typically provide for negotiated fixed hourly rates for specified categories of direct labor plus reimbursement of other direct costs. This type of contract is generally used when there is uncertainty of the extent or duration of the work to be performed by the contractor at the time of contract award or it is not possible to anticipate costs with any reasonable degree of confidence. On T&M contracts, we assume the risk of providing appropriately qualified staff to perform these contracts at the hourly rates set forth in the contracts over their period of performance.
- Firm-fixed price (FFP) contracts provide for a predetermined price for specific solutions. These contracts offer us potential increased profits if we can complete the work at lower costs than planned. While FFP contracts allow us to benefit from cost savings, these contracts also increase our exposure to reduced profits or losses from increased or unexpected costs.

Our earnings and profitability may vary materially depending on changes in the proportionate amount of revenues derived from each type of contract, the nature of services or solutions provided, as well as the achievement of performance objectives and the stage of performance at which the right to receive fees is finally determined. Given the relative amount of risk assumed by the contractor, cost-reimbursement and T&M contracts generally have lower profitability than FFP contracts. For the proportionate amount of revenues derived from each type of contract for the last three fiscal years, see “Other Key Performance Measures—Contract Types” in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Part II of this report.

Selected Financial Data

See “Selected Financial Data” in Part II of this report.

Backlog

Backlog represents the estimated amount of future revenues to be recognized under negotiated contracts as work is performed. Our backlog consists of funded backlog and negotiated unfunded backlog. At January 29, 2016 and January 30, 2015 our total backlog was $7.2 billion and $6.2 billion, respectively. For a complete description of our backlog, see “Other Key Performance Measures—Bookings and Backlog” in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Part II of this report.

Competition

Competition for contracts is intense and we often compete against a large number of established multinational companies which may have greater name recognition, financial resources and larger technical staffs than we do. We also compete against smaller, more specialized companies that concentrate their resources on particular areas, as well as the U.S. government's own capabilities. As a result of the diverse requirements of the U.S. government, we frequently collaborate with other companies to compete for large contracts and bid against these same companies in other situations. Our principal competitors include the following:

- the engineering and technical services divisions of large defense contractors that provide IT services in addition to other hardware systems and products, which include companies such as General Dynamics Corporation, Lockheed Martin Corporation, Northrop Grumman Corporation, L-3 Communications Corporation and Raytheon Company;
- contractors focused principally on technical and IT services, such as Booz Allen Hamilton Inc., Engility Holdings, Inc., CACI International, Inc., ManTech International Corporation, Serco Group plc, Vencore and CSRA Inc.;
- diversified commercial providers that also provide U.S. government IT services, such as Accenture plc, HP Enterprise Services, International Business Machines Corporation and Unisys Corporation; and
- contractors providing supply chain management and other logistics services, such as Agility Logistics Corporation.

We compete on various factors, which include: our technical expertise and qualified and/or security-cleared personnel; our ability to deliver innovative cost-effective solutions in a timely manner; successful program execution on previous programs; our reputation and standing with customers; pricing; and the size and geographic presence of our company.

Competition within the government services industry has intensified which has led to fewer sole-source awards and an increased emphasis on cost competitiveness and affordability. In addition, procurement initiatives to improve efficiency, refocus priorities and enhance best practices could result in fewer new opportunities for our industry as a whole, which would intensify competition within the industry as companies compete for a more limited set of new programs.

Patents and Proprietary Information

Our technical services and solutions are not generally dependent on patent protection, although we do selectively seek patent protection. We claim a proprietary interest in certain of our solutions, software programs, methodologies and know-how. This proprietary information is protected by copyrights, trade secrets, licenses, contracts and other means. We selectively pursue opportunities to license or transfer our technologies to third parties.

In connection with the performance of services, the U.S. government has certain rights to inventions, data, software codes and related material that we develop under U.S. government-funded contracts and subcontracts. Generally, the U.S. government may disclose or license such information to third parties, including, in some instances, our competitors. In the case of some subcontracts that we perform, the prime contractor may also have certain rights to the programs and solutions that we develop under the subcontract.

Research and Development

For information related to our research and development activities, see Note 1 of the notes to the consolidated and combined financial statements contained within this report.

Seasonality

The U.S. government's fiscal year ends on September 30. It is not uncommon for U.S. government agencies to award extra tasks or complete other contract actions leading up to the end of its fiscal year in order to avoid the loss of unexpended fiscal year funds, which may favorably impact our third fiscal quarter. In addition, as a result of a greater number of holidays occurring in our fourth fiscal quarter, as compared to our third fiscal quarter, we may experience sequentially higher revenues in our third fiscal quarter and lower revenues in our fourth fiscal quarter. For selected quarterly financial data, see Note 16 of the notes to the consolidated and combined financial statements contained within this report.

Environmental Matters

Our operations are subject to various foreign, federal, state and local environmental protection and health and safety laws and regulations. Although we do not currently anticipate that compliance costs or the liabilities associated with environmental laws will materially and adversely affect us, we cannot ensure that we will not incur material costs or liabilities in the future. These regulations and risks are described in more detail under "Risk Factors" in this report.

Executive Officers

For information about our executive officers, see "Directors, Executive Officers and Corporate Governance" in Part III of this report.

Company Website and Available Information

Our corporate headquarters is located at 1710 SAIC Drive, McLean, VA 22102. Our phone number is (703) 676-4300 and our homepage on the internet is www.saic.com, which contains information about our Company and operations. Through a link on the Investor Relations section of our website, copies of each of our filings with the Securities and Exchange Commission (SEC) can be viewed and downloaded free of charge as soon as reasonably practicable after the reports and amendments are electronically filed with or furnished to the SEC. The information on our website is not incorporated by reference into and is not a part of this report.

You may also request hard copies of the materials referenced in the preceding paragraph, at no cost, by emailing investor relations at InvestorRelations@saic.com.

Item 1A. Risk Factors

In your evaluation of our Company and business, you should carefully consider the risks and uncertainties described below, together with information included elsewhere within this report and other documents we file with the SEC. The risks and uncertainties described below are those that we have identified as material, but are not the only risks and uncertainties facing us. Our business is also subject to general risks and uncertainties that affect many other companies, such as our ability to collect receivables, overall U.S. and global economic and industry conditions, geopolitical events, changes in laws or accounting rules, fluctuations in interest and exchange rates, terrorism, international conflicts, major health concerns, natural disasters, climate change or other disruptions of expected economic and business conditions. Additional risks and uncertainties not currently known to us or that we currently believe are immaterial also may materially harm our business, financial condition or operating results and result in a decline in the price of our stock. If any of the following risks and uncertainties develop into actual events, our business, financial condition or results of operations could be materially and adversely affected, the trading price of our common stock could decline, and you could lose all or part of your investment.

Risks Relating to Our Business

We depend on U.S. government agencies as our primary customer and, if our reputation or relationships with these agencies were harmed, our future revenues and cash flows would be adversely affected.

We generated either as a prime contractor or a subcontractor to other contractors engaged in work for the U.S. government over 95% of our total revenues during each of the last three fiscal years from contracts with the U.S. government. Moreover, we generated over 60% of our total revenues during each of the last three fiscal years from the DoD, including 29% and 16% of our total revenues in fiscal 2016 from the U.S. Army and U.S. Navy, respectively. We expect to continue to derive substantially all of our revenues from work performed under U.S. government contracts. Our reputation and relationship with the U.S. government, and in particular with the agencies of the DoD, are key factors in maintaining and growing these revenues. Furthermore, each of these agencies has a number of subordinate agencies which have separate budgets and procurement functions and we may also be adversely affected if our reputation or relationships with these subordinate agencies are harmed. Negative press reports or publicity, regardless of accuracy, could harm our reputation. Publicity that could harm our reputation might pertain to employee or subcontractor misconduct, conflicts of interest, poor contract performance, deficiencies in services or other deliverables, information security breaches or other aspects of our business. If our reputation is negatively affected, or if we are suspended or debarred from contracting with government agencies for any reason, the amount of business with government and other customers would decrease and our future revenues, cash flows, and financial results would be adversely affected.

A decline in the U.S. government defense budget, changes in spending or budgetary priorities, the failure to approve U.S. government budgets on a timely basis or delays in contract awards and other procurement activity may significantly and adversely affect our future revenues, cash flow and financial results.

Because we generate substantially all of our revenues from contracts with U.S. government agencies, our operating results could be adversely affected by spending caps or changes in budgetary priorities, as well as by delays in the government budget process, program starts or the award of contracts or task orders under contracts. Current U.S. government spending levels for defense-related and other programs may not be sustained. Future spending and program authorizations may not increase or may decrease or shift to programs in areas in which we do not provide services or are less likely to be awarded contracts. Such changes in spending authorizations and budgetary priorities may occur as a result of shifts in spending priorities from defense-related and other programs as a result of competing demands for federal funds and the number and intensity of military conflicts or other factors.

On November 2, 2015, the President signed the Bipartisan Budget Act of 2015 (the Budget Act). The Budget Act raises the statutory limit on the amount of permissible federal debt (the debt ceiling) until March 2017 and raises the sequestration caps imposed by the Budget Control Act of 2011 (the Budget Control Act) by $80 billion, split equally between defense and domestic spending, over the next two years ($50 billion in government fiscal year (GFY) 2016 and $30 billion in GFY 2017). Sequestration caps initially were put in place for GFY 2013, which resulted in $37 billion in across the board reduction to the defense budget authority. On December 18, 2015, Congress passed and the President signed the Consolidated Appropriations Act of 2016, which provides funding for the U.S. government for FY 2016, providing $1.1 trillion in discretionary funding for federal agencies through September 2016. However, unless Congress and the Administration can reach a new agreement by the end of GFY 2017, the full effect of sequestration will once again take effect in GFY 2018. Further, unforeseen circumstances could cause requested spending to exceed the debt ceiling, which could result in the delay of the U.S. government's timely payment of our billings, resulting in delayed cash collection, and have significant consequences for our company, our employees, our suppliers and the defense industry.

In years when the U.S. government does not complete its budget process before the end of its fiscal year, government operations typically are funded through one or more continuing resolutions that authorize agencies of the U.S. government to continue to operate, but do not authorize new spending initiatives. When the U.S. government operates under a continuing resolution, delays can occur in contract awards due to lack of funding. Continuing resolutions have been used frequently in recent years, including GFY 2016, which operated under this funding mechanism from the October 1, 2015 start of the year until the full appropriations bill was passed on December 18, 2015.

If a continuing resolution is used to fund all or some U.S. government operations after GFY 2016, it may cause additional government contract awards to be delayed, canceled, or funded at lower levels and could adversely impact our operations, cash flows and financial results. Failure to complete its budget or to provide for a continuing resolution may result in a federal government shutdown, which could cause us to incur labor or other costs without reimbursement under customer contracts or the delay or cancellation of key programs, and could adversely impact our operations, cash flows and financial results.

The U.S. government also conducts periodic reviews of U.S. defense strategies and priorities which may shift DoD budgetary priorities, reduce overall spending or delay contract or task order awards for defense-related programs from which we would otherwise expect to derive a significant portion of our future revenues. A significant decline in overall U.S. government spending, a significant shift in spending priorities, the substantial reduction or elimination of particular defense-related programs or significant budget-related delays in contract or task order awards for large programs could adversely affect our future revenues and limit our growth prospects.

Our failure to comply with a variety of complex procurement rules and regulations could result in our being liable for penalties, including termination of our U.S. government contracts, disqualification from bidding on future U.S. government contracts and suspension or debarment from U.S. government contracting.

We must comply with laws and regulations relating to the formation, administration and performance of U.S. government contracts, which affect how we do business with our customers and may impose added costs on our business. Some significant statutes and regulations that affect us include:

- the FAR and agency supplements, which regulate the formation, administration and performance of U.S. government contracts;
- the Truth in Negotiations Act, which requires certification and disclosure of cost or pricing data in connection with certain contract awards;

- the Procurement Integrity Act, which restricts access to competitor bid and proposal information and government source selection information and limits our ability to provide compensation to certain former government officials;
- the Civil False Claims Act, which provides for substantial damages and civil penalties for submission of a false claim to the U.S. government for payment or approval; and
- the U.S. government Cost Accounting Standards (CAS), which impose requirements that govern our right to reimbursement under certain cost-based U.S. government contracts.

Many of our U.S. government contracts contain organizational conflict of interest (OCI) clauses that may limit our ability to compete for or perform certain other contracts or other types of services for particular customers. OCI arises when we engage in activities that may make us unable to render impartial assistance or advice to the U.S. government, impair our objectivity in performing contract work or provide us with an unfair competitive advantage. Existing OCI, and any OCI that may develop, could preclude our competition for or performance on a significant project or contract, which could limit our opportunities.

The U.S. government may adopt new contract rules and regulations or revise its procurement practices in a manner adverse to us at any time.

Our industry continues to experience significant changes to business practices as a result of an increased focus on affordability, efficiencies and recovery of costs, among other items. U.S. government agencies may face restrictions or pressure regarding the type and amount of services that they may obtain from private contractors. Legislation, regulations and initiatives dealing with procurement reform, mitigation of potential OCI's, deterrence of fraud, and environmental responsibility or sustainability could have an adverse effect on us. Moreover, shifts in the buying practices of U.S. government agencies (such as increased usage of fixed price contracts, multiple award contracts and small business set-aside contracts) could have adverse effects on government contractors, including us. Any of these changes could impair our ability to obtain new contracts or contract renewals. Any new contracting requirements or procurement methods could be costly or administratively difficult for us to implement and could adversely affect our future revenues, profitability and prospects.

Our business is subject to reviews, audits and cost adjustments by the U.S. government, which, if resolved unfavorably to us, could adversely affect our profitability, cash flows or growth prospects.

The Defense Contract Audit Agency (DCAA), Defense Contract Management Agency (DCMA) and others routinely audit and review a contractor's performance on government contracts, indirect cost rates and pricing practices, and compliance with applicable contracting and procurement laws, regulations and standards. They also review the adequacy of the contractor's compliance with government standards for its business systems, which are defined as the contractor's accounting, earned value management, estimating, materials management, property management and purchasing systems. A finding of significant control deficiencies in a contractor's business systems or a finding of noncompliance with CAS can result in decremented billing rates to U.S. government customers until the control deficiencies are corrected and their remediation is accepted by the DCMA. The agencies conducting these audits and reviews have come under increased scrutiny. As a result, audits and reviews have become more rigorous and the standards to which we are held are being more strictly interpreted which has increased the likelihood of an audit or review resulting in an adverse outcome.

Government audits and reviews may conclude that our practices are not consistent with applicable laws and regulations and result in adjustments to contract costs and mandatory customer refunds. Such adjustments can be applied retroactively, which could result in significant customer refunds. Receipt of adverse audit findings or the failure to obtain an "approved" determination on our various business systems could significantly and adversely affect our business by, among other things, restricting our ability to bid on new contracts and, for those proposals under evaluation, diminishing our competitive position. A determination of noncompliance could also result in the U.S. government imposing penalties and sanctions against us, including withholding of payments, suspension of payments and increased government scrutiny. Increased scrutiny could adversely impact our ability to perform on contracts, affect our ability to invoice for work performed, delay the receipt of timely payment on contracts, and weaken our ability to compete for new contracts with the U.S. government.

The indirect cost audits by the DCAA of our business remain open for fiscal 2011 and subsequent years. We have recorded contract revenues subsequent to and including fiscal 2011 based on an estimate of costs that we believe will be approved on final audit. However, we do not know the outcome of any ongoing or future audits or whether future adjustments will exceed our reserves for potential adjustments.

We have recorded reserves for estimated net amounts to be refunded to customers for potential adjustments for indirect cost audits and compliance with CAS for indemnification obligations owing to former Parent for periods prior to the spin-off date. Any additional amounts which may be determined to be owed for periods prior to the separation will be allocated to former Parent and us in proportions determined in accordance with the Distribution Agreement. Additional amounts that are allocated to us could have a material, adverse impact to our profitability and cash flows. For a more detailed discussion of the terms of the Distribution Agreement governing financial impacts of audits and reviews for periods prior to the spin-off, see Note 15 of the notes to the consolidated and combined financial statements contained within this report.

Our business is subject to governmental review and investigation which could adversely affect our profitability, cash position and growth prospects.

We are routinely subject to governmental investigations relating to our contracts and operations. If a review or investigation identifies improper or illegal activities, we may be subject to civil or criminal penalties or administrative sanctions which could include the termination of contracts, forfeiture of profits, the triggering of price reduction clauses, suspension of payments, fines, and suspension or debarment from doing business with governmental agencies. We may suffer harm to our reputation if allegations of impropriety are made against us, which would impair our ability to win new contract awards or receive contract renewals. Penalties and sanctions are not uncommon in our industry. If we incur a material penalty or administrative sanction or otherwise suffer harm to our reputation, our profitability, cash position and future prospects could be adversely affected.

The U.S. government may terminate, cancel, modify or curtail our contracts at any time and, if we do not replace them, we may be unable to achieve or sustain revenue growth and may suffer a decline in revenues and profitability.

Many of the U.S. government programs in which we participate as a contractor or subcontractor may extend for several years and include one or more base years and one or more option years. Under our contracts, the U.S. government generally has the right not to exercise options to extend or expand our contracts and may otherwise terminate, cancel, modify or curtail our contracts at its convenience. Any decision by the U.S. government not to exercise contract options or to terminate, cancel, modify or curtail our major programs or contracts would adversely affect our revenues, revenue growth and profitability.

We have experienced and continue to experience periodic performance issues under certain of our contracts. If a government customer terminates a contract for default, we may be exposed to liability, including for excess costs incurred by the customer in procuring undelivered services and solutions from another source. Depending on the nature and value of the contract, a performance issue or termination for default could cause our actual results to differ from those anticipated and could harm our reputation.

We face aggressive competition that can impact our ability to obtain contracts and may affect our future revenues, profitability and growth prospects.

We expect that a majority of the business that we seek in the foreseeable future will be awarded through a competitive bidding process as the U.S. government increasingly relies on IDIQ, GSA Schedule and other multi-award contracts, which has resulted in greater competition and increased pricing pressure. The competitive bidding process involves substantial costs and a number of risks, including significant cost and managerial time to prepare bids and proposals for contracts that may not be awarded to us, or that may be awarded but for which we do not receive meaningful task orders. For contracts awarded to us, we also face the risk of inaccurately estimating the resources and costs that will be required to fulfill any contract we win. Following contract award, we may encounter significant expense, delay, contract modifications or even contract loss as a result of our competitors protesting the award of contracts to us in competitive bidding. Any resulting loss or delay of startup and funding of work under protested contract awards may adversely affect our revenues and/or profitability. In addition, multi-award contracts require that we make sustained post-award efforts to obtain task orders under the contract. As a result, we may not be able to obtain these task orders or recognize revenues under these multi-award contracts. Our failure to compete effectively in this procurement environment would adversely affect our revenues and profitability.

We compete with larger companies that have greater name recognition, financial resources and larger technical staffs and with smaller, more specialized companies that are able to concentrate their resources on particular areas. Additionally, we may compete with the U.S. government's own capabilities.

SCIENCE APPLICATIONS INTERNATIONAL CORPORATION

The markets in which we operate are characterized by both evolving customer needs and rapidly changing technology. Accordingly, our success depends on our ability to develop services and solutions that address these changing needs and to provide the people and technology needed to deliver these services and solutions. To remain competitive, we must consistently provide superior service, technology and performance on a cost-effective basis to our customers. Our competitors may be able to provide customers with different or greater capabilities or technologies or better contract terms than we can provide. They may have better technical qualifications, past contract experience, geographic presence, pricing power and qualified professional personnel. In addition, our competitors may consolidate or establish teaming or other relationships among themselves or with third parties which increases their ability to address customers' needs in a manner that we cannot duplicate. In recent years, certain U.S. government officials have encouraged large, sophisticated commercial technology companies to enter the U.S. government services market. Accordingly, we anticipate that larger or new competitors or alliances among competitors may emerge which may adversely affect our ability to compete for new contracts.

A failure to attract, train, retain and utilize skilled employees and our senior management team would adversely affect our ability to execute our strategy and may disrupt our operations.

Our business relies heavily upon the expertise and services of our employees. Our continued success depends on our ability to recruit and retain highly trained and skilled engineering, technical and professional personnel. Competition for skilled personnel is intense and competitors aggressively recruit key employees. In addition, many U.S. government programs require contractors to have security clearances. Depending on the level of required clearance, security clearances can be difficult and time-consuming to obtain and personnel with security clearances are in great demand. Particularly in highly specialized areas, it has become more difficult to retain employees and meet all of our needs for employees in a timely manner, which may affect our growth in the current and future fiscal years. Although we intend to continue to devote significant resources to recruit, train and retain qualified employees, we may not be able to attract, effectively train and retain these employees. Any failure to do so could impair our ability to efficiently perform our contractual obligations, timely meet our customers' needs and ultimately win new business, all of which could adversely affect our future results.

Salaries and related costs are a significant portion of the cost of providing our services and, accordingly, our ability to efficiently utilize our workforce impacts our profitability. If our employees are under-utilized, our profitability could suffer. The degree to which we are able to utilize our employees in a timely manner or at all is affected by a number of factors including our ability to transition employees from completed projects to new assignments, forecast demand for our services in order to maintain and deploy headcount that is aligned with demand, and our need to devote resources to training, business development, and other non-contract related activities. Additionally, if our employees are over-utilized, it could have an adverse effect on employee engagement and retention, which could, in turn, have an adverse impact on our business.

We believe that our success also depends on the continued employment of a highly qualified and experienced senior management team and that team's ability to retain existing business and generate new business. Our senior management team is important to our business because personal reputations and individual business relationships are a critical element of retaining and obtaining customer contracts in our industry. Moreover, there is little redundancy or overlap of responsibilities in our corporate functions and loss of key personnel in critical functions could lead to lack of business continuity or disruptions in our operations, financial reporting or control processes until we are able to hire and train replacement personnel.

Within the past year, we completed a significant acquisition and may make other acquisitions, investments, joint ventures and divestitures in the future that involve numerous risks, which if realized, may adversely affect our business and our future results.

In May 2015, we acquired Scitor Holdings, Inc. and its subsidiaries (Scitor) for a total purchase price of $764 million, net of cash acquired. In connection with the acquisition, we amended our Credit Facility to incur approximately $670 million of additional debt and converted the Credit Facility from an unsecured facility to a facility secured by a lien on substantially all of our assets. Under the terms of the Credit Facility, we are required to maintain a certain ratio of debt to earnings before interest, taxes, depreciation and amortization (referred to as the Leverage Ratio). Further, under the terms of the Credit Facility, we are limited in our ability to pay dividends beyond our current regular dividend and repurchase shares of our stock above a certain Leverage Ratio, are required to make certain mandatory prepayments based on the cash flow of our business, and are subject to other operational limitations.

Our Credit Facility also imposes limitations on our ability to make other acquisitions. Subject to those limitations, we may selectively pursue additional strategic acquisitions, investments and joint ventures. The Scitor acquisition and other acquisitions, investments and joint ventures pose many risks that could adversely affect our reputation, operations or financial results, including:

- we may not retain key employees (including those with needed security clearances), customers and business partners of Scitor or those of an acquired business in the future;
- we may fail to successfully integrate Scitor or other future acquired businesses, such as failing to successfully implement IT and other control systems relating to the operations of Scitor or any other future acquired business;
- we may not generate sufficient earnings to meet the required Leverage Ratio under the Credit Facility, which would give lenders the right to, among other things, foreclose on our assets;
- even if successful, the Scitor acquisition and any future acquisition could reduce our earnings per share or net income for a number of reasons, including the amortization of intangible assets, impairment charges, the inability to generate or sustain profits of the acquired business, adverse changes in unhedged interest rates on debt incurred to complete the acquisition or a failure to realize assumed future tax benefits estimated in connection with the acquisition;
- acquisitions normally require a significant investment of time and resources, which may disrupt our business and distract our management from other important responsibilities;
- the limitations on our ability to issue dividends beyond our current regular dividend and to repurchase our stock under the Credit Facility above a certain Leverage Ratio may restrict our capital deployment decisions in the future, which may have an adverse impact on our stock price;
- we may not be able to accurately estimate the financial effect of the Scitor acquisition or any future acquisitions and investments on our business and we may not realize anticipated revenue opportunities, cost savings, or other synergies or benefits, or acquisitions may not result in improved operating performance;
- we may assume known as well as unknown material liabilities that were not identified as part of our due diligence or for which we are unable to receive a purchase price adjustment or reimbursement through indemnification;
- we may assume legal or regulatory risks, particularly with respect to businesses that have immature business processes and compliance programs or that operate in markets in which we have previously had limited direct prior experience;
- we may be adversely impacted by developments in the U.S. government intelligence community budgets and other areas to which we had limited exposure prior to the acquisition;
- we may encounter performance problems with acquired technologies, capabilities and products, particularly with respect to those that are still in development when acquired;
- acquired entities or joint ventures may not operate profitably, which could adversely affect our operating income or operating margins and we may be unable to recover investments in any such acquisitions;
- acquisitions, investments and joint ventures may require us to spend a significant amount of cash and incur a substantial amount of debt, with increased interest expense and amortization demands and mandatory prepayment requirements, or to issue capital stock, resulting in dilution of ownership; and
- we may not be able to effectively influence the operations of our joint ventures or we may be exposed to certain liabilities if our joint venture partners do not fulfill their obligations or fail to comply with legal requirements, laws and regulations.

If the Scitor acquisition or any other acquisitions, investments or joint ventures fail, perform poorly or their value is otherwise impaired for any reason, including contractions in credit markets and global economic conditions, our business and financial results would be adversely affected.

In addition, we may periodically divest businesses, including businesses that are no longer a part of our ongoing strategic plan. These divestitures similarly require significant investment of time and resources and may disrupt our business, distract management from other responsibilities and may result in losses on disposal or continued financial involvement in the divested business, including through indemnification, guarantee or other financial arrangements, for a period of time following the transaction, which could adversely affect our financial results.

We may not realize as revenues the entire amounts reflected in our backlog, which could adversely affect our expected future revenues and growth prospects.

As of January 29, 2016, our total backlog was $7.2 billion, which included $1.9 billion in funded backlog. Due to the U.S. government’s ability to not exercise contract options or to terminate, modify or curtail our programs or contracts and the rights of our non-U.S. government customers to cancel contracts and purchase orders in certain circumstances, we may realize less than expected or, in some cases, never realize revenues from some of the contracts that are included in our backlog. Our unfunded backlog, in particular, contains management’s estimate of amounts expected to be realized on unfunded contract work that may never be realized as revenues. If we fail to realize as revenues amounts included in our backlog, our expected future revenues, growth prospects and profitability could be adversely affected.

Our earnings and profitability may vary based on the mix of our contracts and may be adversely affected by our failure to accurately estimate and manage costs, time and resources.

We generate revenues under various types of contracts, which include cost-reimbursement, T&M and FFP contracts. Our earnings and profitability may vary materially depending on changes in the proportionate amount of revenues derived from each type of contract, the nature of services or solutions provided, as well as the achievement of performance objectives and the stage of performance at which the right to receive fees, particularly under incentive and award fee contracts, is finally determined. Cost-reimbursement and T&M contracts generally have lower profitability than FFP contracts.

To varying degrees, each of our contract types involves some risk that we could underestimate the costs and resources necessary to fulfill the contract. Our profitability is adversely affected when we incur costs on cost-reimbursement and T&M contracts that we cannot bill to our customers. While FFP contracts allow us to benefit from cost savings, these contracts also increase our exposure to the risk of cost overruns. Revenues derived from FFP contracts represented approximately 32% of our total revenues for fiscal 2016. When making proposals on FFP contracts, we rely heavily on our estimates of costs and timing for completing the associated projects, as well as assumptions regarding technical issues. In each case, our failure to accurately estimate costs or the resources and technology needed to perform our contracts or to effectively manage and control our costs during the performance of work could result, and in some instances has resulted, in reduced profits or in losses. More generally, any increased or unexpected costs or unanticipated delays in connection with the performance of our contracts, including costs and delays caused by contractual disputes or other factors outside of our control (such as performance failures of our subcontractors, natural disasters or other force majeure events) could make our contracts less profitable than expected or unprofitable.

We use estimates in recognizing revenues and, if we make changes to estimates used in recognizing revenues, our profitability may be adversely affected.

A significant portion of our contract revenues are recognized using the percentage-of-completion method. This method requires estimates of total costs at completion, fees earned on the contract, or both. Particularly due to the technical nature of the services being performed and the length of certain contracts, this estimation process is complex and involves significant judgment. Adjustments to original estimates are often required as work progresses, experience is gained and additional information becomes known, even though the scope of the work required under the contract may not change. Any adjustment as a result of a change in estimate is recognized immediately. Changes in the underlying assumptions, circumstances or estimates could result in adjustments that may adversely affect future financial results.

Our business and financial results could be negatively affected by cyber or other security threats.

As a U.S. government contractor and a provider of IT services operating in multiple regulated industries and geographies, we handle sensitive information which includes personally identifiable information, protected health information, personnel information, classified information, financial information and other confidential information concerning our business and employees and those of our customers (collectively referred to below as sensitive information). We are continuously exposed to cyber and other security threats, including computer viruses, attacks by hackers or physical break-ins. Any electronic or physical break-in or other security breach or compromise may jeopardize security of sensitive or other information stored or transmitted through our IT systems and networks. This could lead to disruptions in mission critical systems, unauthorized release of confidential or otherwise protected information and corruption of data. Although we have implemented policies, procedures and controls to protect against, detect and mitigate these threats, attempts by others to gain unauthorized access to our IT systems are becoming more sophisticated. These attempts include covertly introducing malware to our computers and networks and impersonating authorized users, among others, and may be perpetrated by well-funded organized crime or state sponsored efforts. We seek to detect and investigate all security events and to prevent their occurrence or recurrence. We continue to improve our threat protection, detection and mitigation policies, procedures and controls.

In addition, we work with other companies in the industry and government participants to share threat intelligence and promote increased awareness and enhanced protections against cybersecurity threats. However, because of the evolving nature of these security threats, there can be no assurance that our policies, procedures and controls have or will detect or prevent any of these threats and we cannot predict the full impact of any such incident. We may experience similar security threats to the IT systems that we develop, install or maintain under customer contracts, including customer contracts under which we may have access to or management responsibility for customer databases or networks that contain sensitive information relating to our customers, their employees or related third parties. Although we work cooperatively with our customers and other business partners to seek to minimize the impacts of cyber and other security threats, we must rely on the safeguards put in place by those entities.

In the event of unauthorized access to sensitive information that we are responsible for safeguarding, our customers and their employees or related third parties, if applicable, may seek to hold us liable for any costs or other damages associated with the unauthorized access as a breach of our contractual and other obligations. In addition, various federal or state agencies may bring legal action against us for violation of or noncompliance with regulatory requirements relating to any unauthorized access to sensitive information within our control. Any remediation costs, damages or other liabilities related to unauthorized access of sensitive information of ours or our customers caused by cyber or other security threats may not be fully insured or indemnified by other means. Occurrence of any unauthorized access caused by these security threats could adversely affect our reputation, ability to work on sensitive U.S. government contracts, business operations and financial results.

Internal system or service failures could disrupt our business and impair our ability to effectively provide our services and solutions to our customers, which could damage our reputation and adversely affect our revenues and profitability.

Any internal disruption or failure in our IT network, software or hardware systems, communications equipment, utilities or other business equipment or services could have a material adverse effect on our ability to provide the services required to be performed by us under customer contracts or bill our customers for work performed, collect the amounts that have been billed and produce accurate financial statements in a timely manner. We are also vulnerable to failures in these systems, equipment and other business services caused by third-party service providers, cybersecurity threats, natural disasters, power shortages, terrorist attacks or other events, which could cause loss of data and interruptions or delays in our business, cause us to incur remediation costs, subject us to claims and damage our reputation. In addition, the failure or disruption of our communications or utilities could cause us to interrupt or suspend our operations or otherwise adversely affect our business. Our property and business interruption insurance may be inadequate to compensate us for all losses that may occur as a result of any system or operational failure or disruption. As a result, any internal or external disruption or failure in our IT network, software or hardware systems, communications equipment, utilities or other business equipment or services could damage our reputation and adversely affect our revenues and profitability.

Customer systems failures could damage our reputation and adversely affect our revenues and profitability.

Many of the systems and networks that we develop, install and maintain for our customers involve managing and protecting personal information and information relating to national security and other sensitive government functions. While we have programs designed to comply with relevant privacy and security laws and restrictions, if a system or network that we develop, install or maintain were to fail or experience a security breach or service interruption, whether caused by us, third-party service providers, cybersecurity threats or other events, we may experience loss of revenue, remediation costs or face claims for damages or contract termination. Any such event could cause serious harm to our reputation and prevent us from having access to or being eligible for further work on such systems and networks. Our errors and omissions liability insurance may be inadequate to compensate us for all of the damages that we may incur and, as a result, our future results could be adversely affected.

Legal disputes could require us to pay potentially large damage awards and could be costly to defend, which would adversely affect our cash balances and profitability, and could damage our reputation.

We are subject to a number of lawsuits and claims described under “Legal Proceedings” in Part I of this report. We are also subject to, and may become a party to, a variety of other litigation or claims and suits that arise from time to time in the ordinary course of our business. The Department of Justice and other enforcement agencies of the U.S. government may bring claims or lawsuits against us in connection with our performance of government contracts or our billing or record-keeping relating to those contracts. The Department of Justice has considerably more resources at its disposal than we do, and can bring suspension and debarment proceedings against us that would prevent us from working for some or all U.S. government customers. In addition, certain statutes under which the Department of Justice may bring claims (like the False Claims Act) provide for treble damages and penalties on a per invoice basis against government contractors. These circumstances generally give the Department of Justice significantly more leverage in any legal dispute with us than if we were defending ourselves against claims brought by a commercial enterprise. Adverse judgments or settlements in some or all of these legal disputes may result in significant monetary damages or injunctive relief against us. Any claims or litigation could be costly to defend, and even if we are successful or if fully indemnified or insured, could damage our reputation and make it more difficult to compete effectively or obtain adequate insurance in the future. Litigation and other claims, including those described under “Legal Proceedings” in Part I of this report, are subject to inherent uncertainties and management’s view of these matters may change in the future.

Our business is subject to numerous legal and regulatory requirements and any violation of these requirements or any misconduct by our employees, subcontractors, agents or business partners could harm our business and reputation.

In addition to government contract procurement laws and regulations, we are subject to numerous other federal, state and foreign legal requirements on matters as diverse as data privacy and protection, employment and labor relations, immigration, taxation, anti-corruption, import/export controls, trade restrictions, internal and disclosure control obligations, securities regulation and anti-competition. Compliance with diverse and changing legal requirements is costly, time-consuming and requires significant resources. Violations of one or more of these requirements in the conduct of our business could result in significant fines and other damages, criminal sanctions against us or our officers, prohibitions on doing business and damage to our reputation. Violations of these regulations or contractual obligations related to regulatory compliance in connection with the performance of customer contracts could also result in liability for significant monetary damages, fines and/or criminal prosecution, unfavorable publicity and other reputational damage, restrictions on our ability to compete for certain work and allegations by our customers that we have not performed our contractual obligations.

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Misconduct by our employees, subcontractors, agents or business partners could harm our business. Such misconduct could include fraud or other improper activities such as falsifying time or other records, failure to comply with our policies and procedures or violations of applicable laws and regulations. Although we have implemented policies, procedures and controls to prevent and detect these activities, our precautions may not prevent all misconduct and, as a result, we could face unknown risks or losses. Misconduct by any of our employees, subcontractors, agents or business partners could damage our reputation and subject us to fines and penalties, restitution or other damages, loss of security clearance, loss of current and future customer contracts and suspension or debarment from contracting with federal, state or local government agencies, any of which would adversely affect our business and our future results.

Our reputation may be harmed or other adverse consequences may be incurred by us relating to former Parent's CityTime contract, which could have a material adverse effect on our business and future prospects.

In connection with the resolution of certain investigations related to former Parent's CityTime contract, former Parent entered into a deferred prosecution agreement with the U.S. Attorney's Office for the Southern District of New York and an administrative agreement with the Army on behalf of the U.S. government to confirm former Parent's continuing eligibility to enter into and perform contracts with the U.S. government. While both of these agreements have terminated, given that we have retained the name Science Applications International Corporation, which was the name of the company that was the prime contractor under the CityTime contract, we may suffer reputational harm as a result of being associated with the contract as well as with former Parent's deferred prosecution agreement and administrative agreement. This could make it more difficult to compete effectively and may adversely affect our future revenues and growth prospects.

Goodwill and intangible assets represent a significant amount of our total assets and any impairment of these assets would negatively impact our results of operations.

In May 2015 we completed the acquisition of Scitor Holdings, Inc. and its subsidiaries for purchase consideration of $764 million. As a result, goodwill and intangible assets have increased significantly following completion of this acquisition. Goodwill and intangible assets are tested for impairment annually or whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Examples of events or changes in circumstances indicating that the carrying value of goodwill may not be recoverable could include a significant adverse change in legal factors or in the business climate, an adverse action or assessment by a regulator, unanticipated competition, loss of key personnel or a more likely than not expectation that a reporting unit or a significant portion of a reporting unit will be sold or otherwise disposed of. Any future impairment of goodwill or other intangible assets would have a negative impact on our profitability and financial results.

We depend on our teaming arrangements and relationships with other contractors and subcontractors. If we are not able to maintain these relationships, or if these parties fail to satisfy their obligations to us or the customer, our revenues, profitability and growth prospects could be adversely affected.

We rely on teaming relationships with other prime contractors and subcontractors in order to submit bids for large procurements or other opportunities where we believe the combination of services, products and solutions provided by us and our teammates will help us to win and perform the contract. Our future revenues and growth prospects could be adversely affected if other contractors eliminate or reduce their contract relationships with us, or if the U.S. government terminates or reduces these other contractors' programs, does not award them new contracts or refuses to pay under a contract. Companies that do not have access to U.S. government contracts or experience with our customers may perform services as our subcontractor that we cannot otherwise provide ourselves, and that exposure could enhance such companies' prospect of securing a future position as a prime U.S. government contractor which could increase competition for future contracts and impair our ability to win these contracts.

From time to time, we have disputes with our subcontractors arising from, among other things, the quality and timeliness of work performed, customer concerns about the subcontractor, our failure to extend existing task orders or issue new task orders under a subcontract, our hiring of a subcontractor's personnel or the subcontractor's failure to comply with applicable law. Any financial stress of our subcontractors could adversely impact their ability to meet their contractual requirements to us. If any of our subcontractors fail to timely meet their contractual obligations, have regulatory compliance or other problems, our ability to fulfill our obligations as a prime contractor or higher tier subcontractor may be jeopardized. In addition, we have certain obligations to our former Parent to permit it to perform up to one hundred percent (100%) of task orders as a subcontractor to us under certain contracts that were novated to us in the spin-off transaction. Subcontractor performance deficiencies under subcontracts with us as the prime contractor, including performance by our former Parent, could lead to significant losses in future periods and could result in our termination for default as the prime contractor even though it was the subcontractor that failed to perform and not our personnel. A termination for default could eliminate a revenue source, expose us to liability, hurt our reputation with customers and have an adverse effect on our ability to compete for future contracts and task orders, especially if the customer is an agency of the U.S. government.

We have only a limited ability to protect our intellectual property rights, which are important to our success. Our failure to adequately protect our proprietary information and intellectual property rights could adversely affect our competitive position.

We rely principally on trade secrets to protect much of our intellectual property in cases where we do not believe that patent protection is appropriate or obtainable. However, trade secrets are difficult to protect. Although our employees are subject to confidentiality obligations, this protection may be inadequate to deter or prevent misappropriation of our confidential information. We may be unable to detect unauthorized use of our intellectual property or otherwise take appropriate steps to enforce our rights. Failure to obtain or maintain trade secret protection could adversely affect our competitive business position. If we are unable to prevent third parties from infringing or misappropriating our copyrights, trademarks or other proprietary information, our competitive position could be adversely affected. In addition, in connection with the performance of services, the U.S. government has certain rights to inventions, data, software codes and related material that we develop under government-funded contracts and subcontracts, which may permit the U.S. government to disclose or license this information to third parties, including, in some instances, our competitors.

In the course of conducting our business, we may inadvertently infringe the intellectual property rights of others, resulting in claims against us or our customers. Our contracts generally indemnify our customers for third-party claims for intellectual property infringement by the services and solutions we provide. The expense of defending these claims may adversely affect our financial results.

Our insurance may be insufficient to protect us from claims or losses.

We maintain insurance coverage with third-party insurers as part of our overall risk management strategy and because some of our contracts require us to maintain specific insurance coverage limits. However, not every risk or liability is or can be protected by insurance, and, for those risks we insure, the limits of coverage we purchase or that are reasonably obtainable in the market may not be sufficient to cover all actual losses or liabilities incurred. If any of our third-party insurers fail, cancel our coverage or otherwise are unable to provide us with adequate insurance coverage, then our overall risk exposure and our operational expenses would increase and the management of our business operations could be disrupted. Our insurance may be insufficient to protect us from significant warranty and other liability claims or losses. Moreover, there is a risk that commercially available liability insurance will not continue to be available to us at a reasonable cost, if at all. If liability claims or losses exceed our current or available insurance coverage, our business and prospects may be harmed. Regardless of the adequacy of our insurance coverage, any significant claim could have an adverse impact on our market reputation, which could have an adverse impact on our ability to compete for future contracts and task orders.

We could incur significant liabilities and suffer negative publicity if our detection systems fail to operate as intended or our assessment reports prove to be inaccurate.

We have developed and sold tsunami buoys and related services that are designed to assist in the detection of tsunamis or large waves that may have catastrophic consequences to coastal communities. Our buoys have been deployed by the U.S. National Oceanic and Atmospheric Administration and non-U.S. governments in other areas around the world. There are many factors, some of which are beyond our control, which could result in the failure of these buoys. We may develop other products or provide services for the detection of natural or manmade threats that could have catastrophic consequences if the threats are realized. In addition, we prepare reports for various government customers in the evaluation or assessment of the consequences of certain threats or natural disasters. The failure of our products and services to help detect the threats for which they were designed or the failure of our reports to accurately assess the consequences of certain threats could contribute to injury, death and extensive property damage and may lead to product liability, professional liability, or other claims against us. Further, if our products, services or reports fail to, or are perceived to have failed to help detect or adequately assess a threat, the negative publicity from such incident could have a material adverse effect on our business.

Our services and operations sometimes involve using, handling or disposing of hazardous substances or dangerous materials, which could expose us to potentially significant liabilities.

Some of our services and operations involve the use, handling or disposal of hazardous substances or dangerous materials, including explosive, chemical, biological, radiological or nuclear materials. These activities generally subject us to extensive foreign, federal, state and local environmental protection and health and safety laws and regulations, which, among other things, require us to incur costs to comply with these regulations and could impose liability on us for handling or disposing of hazardous substances or dangerous materials. Furthermore, failure to comply with these environmental protection and health and safety laws and regulations could result in civil, criminal, regulatory, administrative or contractual sanctions, including fines, penalties or suspension or debarment from contracting with the U.S. government or could cause us to incur costs to change, upgrade, remediate and/or close some of our operations or properties. Although we do not have extensive real estate holdings, our ownership and operation of real property also subjects us to environmental protection laws, some of which hold current or previous owners or operators of businesses and real property liable for hazardous substance releases, even if they did not know of and were not responsible for the releases. If we have any violations of, or incur liabilities pursuant to, these laws or regulations, our financial condition and operating results could be adversely affected.

We face risks associated with our international business.

Our international business operations may be subject to additional and different risks than our U.S. business. Failure to comply with U.S. government laws and regulations applicable to international business such as the Foreign Corrupt Practices Act or U.S. export control regulations could have an adverse impact on our business with the U.S. government and could expose us to administrative, civil or criminal penalties and may expose us to potentially significant contract losses. In addition, we provide services and solutions in support of U.S. government customers in countries with governments that may be or may become unstable or are in areas of active military or intelligence operations. Operating in such environments may increase the risk of an incident resulting in injury or loss of life, or damage or destruction of property, or inability to meet our contractual obligations. Although our international operations have historically generated a small proportion of our revenues, we do not know the impact that these regulatory, geopolitical and other factors may have on our business in the future and any of these factors could adversely affect our business.

Risks Relating to our Stock

Provisions in our organizational documents and Delaware law could delay or prevent transactions that many stockholders may favor.

Some provisions of our certificate of incorporation and bylaws may have the effect of delaying, discouraging or preventing a merger or acquisition that our stockholders may consider favorable, including transactions in which stockholders might receive a premium for their shares. These restrictions, which may also make it more difficult for our stockholders to elect directors not endorsed by our current directors and management, include the following:

- Our certificate of incorporation provides that our bylaws and certain provisions of our certificate of incorporation may be amended by only two-thirds or more voting power of all of the outstanding shares entitled to vote. These supermajority voting requirements could impede our stockholders’ ability to make changes to our certificate of incorporation and bylaws.
- Our certificate of incorporation contains certain supermajority voting provisions, which generally provide that mergers and certain other business combinations between a related person and us be approved by the holders of securities having at least 80% of our outstanding voting power, as well as by the holders of a majority of the voting power of such securities that are not owned by the related person.
- Our stockholders may not act by written consent. As a result, a holder, or holders, controlling a majority of our stock are limited in their ability to take certain actions other than in connection with the annual stockholders’ meeting or a special meeting called at the request of qualified stockholders as provided in our certificate of incorporation and bylaws.
- Our Board of Directors may issue, without stockholder approval, shares of undesignated preferred stock. The ability to authorize undesignated preferred stock makes it possible for our Board of Directors to issue preferred stock with voting or other rights or preferences that could impede the success of any attempt to acquire us.

As a Delaware corporation, we are also subject to certain restrictions on business combinations. Under Delaware law, a corporation may not engage in a business combination with any holder of 15% or more of its stock unless the holder has held the stock for three years, or among other things, our Board of Directors has approved the business combination or the transaction pursuant to which such person became a 15% holder prior to the time the person became a 15% holder.

We have contracts with the U.S. government that are classified which may limit investor insight into portions of our business.

We derive a portion of our revenues from programs with the U.S. government that are subject to security restrictions (classified programs), which preclude the dissemination of information that is classified for national security purposes. We are limited in our ability to provide information about these classified programs, their risks or any disputes or claims relating to such programs. As a result, investors have less insight into our classified programs than our other programs and therefore less ability to fully evaluate the risks related to our classified business.

We cannot assure you that we will pay dividends on our stock in the future.

The Board of Directors authorized and declared a quarterly cash dividend for each of the quarters since the spin-off from former Parent. The declaration of any future dividends and the establishment of the per share amount, record dates and payment dates for any future dividends are subject to the discretion of the Board of Directors taking into account future earnings, cash flows, financial requirements and other factors. There can be no assurance that the Board of Directors will declare any dividends in the future. In addition, our ability to declare and pay any future dividends may be restricted by the provisions of Delaware law and covenants in our Credit Facility. To the extent that expectations by market participants regarding the potential payment, or amount, of any dividend prove to be incorrect, the price of our common stock may be materially and negatively affected and investors that bought shares of our common stock based on those expectations may suffer a loss on their investment.

Forward-Looking Statement Risks

You may not be able to rely on forward-looking statements.

This report contains forward-looking statements that are based on our management’s belief and assumptions about the future in light of information currently available to our management. In some cases, you can identify forward-looking statements by words such as “may,” “will,” “should,” “expects,” “projects,” “intends,” “plans,” “anticipates,” “believes,” “esti
“predicts,” “potential,” “continue,” “outlook,” and similar words or phrases or the negative of these words or phrases. These statements relate to future events or our future financial performance, and involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements. Although we believe that the expectations reflected in the forward-looking statements are reasonable when made, we cannot guarantee future results, levels of activity, performance or achievements. There are a number of important factors that could cause our actual results to differ materially from those results anticipated by our forward-looking statements, which include, but are not limited to the risk factors discussed above.

We do not undertake any obligation to update or revise any of the forward-looking statements to reflect events, circumstances, changes in expectations, or the occurrence of unanticipated events after the date of those statements or to conform these statements to actual results.

Item 1B. Unresolved Staff Comments

No information is required in response to this item.

Item 2. Properties

We occupy approximately 3 million square feet of floor space, substantially all of which is leased. Our corporate headquarters is located in McLean, Virginia. Our principal locations outside of McLean, Virginia include Reston, VA, Chantilly, VA, Huntsville, Alabama and Oak Ridge, Tennessee. As of January 29, 2016, we conducted our operations in approximately 100 offices located in 30 states, the District of Columbia, and various foreign countries. We consider our facilities suitable and adequate for our present needs, which are generally limited to office, warehouse and computer laboratory spaces.

Item 3. Legal Proceedings

We have provided information about legal proceedings in which we are involved in Note 15 of the notes to the consolidated and combined financial statements contained within this report.

We are also routinely subject to investigations and reviews relating to compliance with various laws and regulations. Additional information regarding such investigations and reviews is described under the heading “Government Investigations, Audits and Reviews” in Note 15 of the notes to the consolidated and combined financial statements contained within this report.

Item 4. Mine Safety Disclosures

No information is required in response to this item.

Part II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchase of Equity Securities

Holders of Common Stock, Historical Prices and Dividends

Our common stock is listed on the New York Stock Exchange under the ticker symbol "SAIC" and started trading on September 30, 2013. Prior to September 30, 2013, there was no public market for our common stock. The following table presents, for the periods indicated, the high and low prices for our common stock as reported in the consolidated reporting system for the New York Stock Exchange Composite Transactions:

	Fiscal 2016	Fiscal 2015
First Quarter	$48.78 to $55.70	$34.65 to $39.73
Second Quarter	$49.83 to $54.19	$36.64 to $45.64
Third Quarter	$39.89 to $53.69	$41.37 to $48.91
Fourth Quarter	$40.87 to $51.60	$48.78 to $52.13

As of March 4, 2016, there were approximately 30,000 holders of record of our common stock. The number of holders of record of our common stock may not be representative of the number of beneficial owners due to shares that may be held by depositories, brokers or nominees.

Quarterly dividends per common share declared for the most recent two fiscal years are as follows:

	Fiscal 2016	Fiscal 2015
First Quarter	$0.28	$0.28
Second Quarter	$0.31	$0.28
Third Quarter	$0.31	$0.28
Fourth Quarter	$0.31	$0.28

We intend to continue paying dividends on a quarterly basis, although the declaration of any future dividends will be determined by our Board of Directors and will depend on available cash, estimated cash needs, earnings, financial condition, operating results, capital requirements, applicable contractual restrictions and other factors that our Board of Directors deems relevant. In addition, our ability to declare and pay future dividends on our stock may be restricted by the provisions of Delaware law and covenants in our Credit Facility.

Stock Performance Graph

The following graph compares the total cumulative return on our common stock from September 30, 2013 (the date on which our stock began trading) through fiscal 2016 to three indices: (i) the Standard & Poor's (S&P) MIDCAP 400 Index, (ii) the Russell 1000 Index and (iii) the S&P North American Technology Services Index. The graph assumes an initial investment of $100 on September 30, 2013 and that dividends have been reinvested. The comparisons in the graph are required by the U.S. Securities and Exchange Commission (SEC), based upon historical data and are not intended to forecast or be indicative of possible future performance of our common stock.

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Purchases of Equity Securities

We may repurchase shares on the open market in accordance with established repurchase plans. Whether repurchases are made and the timing and amount of repurchases depend on a variety of factors including market conditions, our capital position, internal cash generation and other factors.

The following table presents repurchases of our common stock during the three months ended January 29, 2016:

Period (1)	Total Number of Shares (or Units) Purchased (2)	Average Price Paid per Share (or Unit)	Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs (3)
October 31, 2015 - December 4, 2015	265,928	$ 47.39	263,808	4,305,051
December 5, 2015 - January 1, 2016	201,055	46.62	200,818	4,104,233
January 2, 2016 - January 29, 2016	230,918	43.14	230,107	3,874,126
Total	697,901	$ 45.76	694,733	

(1) Date ranges represent our fiscal periods during the current quarter. Our fiscal quarters typically consist of one five-week period and two four-week periods.

(2) Includes shares purchased on surrender by stockholders of previously owned shares to satisfy minimum statutory tax withholding obligations related to stock option exercises and vesting of stock awards in addition to shares purchased under our publicly announced plans or programs.

(3) On September 11, 2015 the number of additional shares of our common stock that may be repurchased under our existing repurchase program previously announced in October 2013 was increased by approximately 3.5 million shares, bringing the total authorized shares to be repurchased under the program to approximately 8.5 million shares. As of January 29, 2016, we have repurchased approximately 4.7 million shares of common stock under the program.

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Item 6. Selected Financial Data

We commenced operations on September 27, 2013 following completion of a spin-off transaction from our former parent, Leidos Holdings, Inc. (collectively with its consolidated subsidiaries, "former Parent"). Our consolidated and combined statement of income data for fiscal years 2012 and 2013 consist entirely of the combined results of the technical, engineering and enterprise information technology (IT) services business of former Parent. Our consolidated and combined balance sheet data as of the end of fiscal years 2012 and 2013 has been reflected on a historical basis from records maintained by former Parent, as prior to the separation all of the assets and liabilities presented were wholly-owned by former Parent. For fiscal 2014, our consolidated and combined statement of income data consists of the combined results of the technical, engineering and enterprise IT services business of former Parent through separation and our consolidated results subsequent to separation. Our consolidated balance sheet data at January 31, 2014 consists of our consolidated balances.

On May 4, 2015, we acquired 100% of privately held Scitor Holdings, Inc. (Scitor) and the consolidated and combined statement of income data includes the results of the operations of Scitor subsequent to the acquisition.

This information should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated and combined financial statements and the notes thereto contained within this report.

	Year Ended				
	January 29, 2016	January 30, 2015	January 31, 2014	January 31, 2013	January 31, 2012
	(in millions, except per share data)				
Consolidated and Combined Statement of Income Data:					
Total revenues	$4,315	$3,885	$4,121	$4,781	$4,733
Operating income	227	240	183	281	299
Net income	117	141	113	182	182
Earnings per share(a):					
Basic	$2.55	$3.01	$2.33	$3.74	$3.74
Diluted	$2.47	$2.91	$2.27	$3.66	$3.66
Cash dividend per share	$1.21	$1.12	$0.56	$-	$-

	January 29, 2016	January 30, 2015	January 31, 2014	January 31, 2013	January 31, 2012
Consolidated and Combined Balance Sheet Data:					
Total assets(b),(c)	$2,122	$1,389	$1,442	$1,229	$1,360
Long-term debt and capital lease obligations, including current portion(b)	1,070	486	498	3	7
Other long-term liabilities and deferred income taxes(c)	41	38	31	10	9

(a) For more information on the calculation of Basic and Diluted Earnings per share see Note 2 of the notes to the consolidated and combined financial statements contained within this report.

(b)

Total assets and long-term debt and capital lease obligations (including current portion) have been restated to reflect the retrospective application of ASU 2015-03, Interest – Imputation of Interest (Subtopic 835-30), which the Company early adopted during the second quarter of fiscal 2016. See Note 1 of the notes to the consolidated and combined financial statements contained within this report.

(c) Total assets and other long-term liabilities and deferred income taxes have been restated to reflect the retrospective application of ASU 2015-17, Income Taxes (Topic 740), Balance Sheet Classification of Deferred Taxes, which the Company early adopted during the fourth quarter of fiscal 2016. See Note 1 of the notes to the consolidated and combined financial statements contained within this report.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis of our financial condition and results of operations, and quantitative and qualitative disclosures about market risk should be read in conjunction with our consolidated and combined financial statements and the related notes. It contains forward-looking statements (which may be identified by words such as those described in "Risk Factors—Forward-Looking Statement Risks" in Part I of this report), including statements regarding our intent, belief, or current expectations with respect to, among other things: trends affecting our financial condition or results of operations (including our financial targets discussed below under "Management of Operating Performance and Reporting" and "Liquidity and Capital Resources"); backlog; our industry; government budgets and spending; the impact of competition; and the impact of the Scitor acquisition. Such statements are not guarantees of future performance and involve risks and uncertainties, and actual results may differ materially from those in the forward-looking statements as a result of various factors. Factors that could cause or contribute to these differences include those discussed below and elsewhere in this report, particularly in "Risk Factors" in Part I of this report. Due to such uncertainties and risks, you are cautioned not to place undue reliance on such forward-looking statements, which speak only as of the date hereof. We do not undertake any obligation to update these factors or to publicly announce the results of any changes to our forward-looking statements due to future results or developments.

References herein to "former Parent" refer to Leidos Holdings, Inc. (formerly SAIC, Inc.) collectively with its consolidated subsidiaries. We use the terms "Company," "we," "us" and "our" to refer to both (1) Science Applications International Corporation and its consolidated subsidiaries for time periods after the separation and (2), for time periods prior to separation, the technical, engineering and enterprise information technology (IT) services businesses of former Parent, which were contributed to Science Applications International Corporation as part of the separation. The financial information discussed below and included elsewhere in this report may not necessarily reflect what our financial condition, results of operations or cash flow would have been had we been a stand-alone company during the periods presented prior to separation or what our financial condition, results of operations and cash flows may be in the future.

The Company utilizes a 52/53 week fiscal year, ending on the Friday closest to January 31, with fiscal quarters typically consisting of 13 weeks. Fiscal 2014 began on February 1, 2013 and ended on January 31, 2014, fiscal 2015 began on February 1, 2014 and ended on January 30, 2015, and fiscal 2016 began on January 31, 2015 and ended on January 29, 2016.

Business Overview

We are a leading technology integrator providing full life cycle services and solutions in the technical, engineering, intelligence and enterprise IT markets. Whether prior to the separation or as a separate company today, our brand was developed through over 45 years of continuously addressing customers' mission critical needs and solving their most complex problems. As one of the largest pure-play technical service providers to the U.S. government, we serve markets of significant scale and opportunity, with our primary customers being the departments and agencies of the U.S. government. We serve our customers through approximately 1,700 active contracts and task orders and employ approximately 15,000 individuals who are led by an experienced executive team of proven industry leaders. Serving our country's national security and civilian markets, along with commercial customers and state and local governments, has afforded us the ability to develop strong and longstanding relationships with some of the largest customers in the markets we serve.

Substantially all of our revenues are generated by, and tangible long-lived assets owned by, entities located in the United States.

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Economic Opportunities, Challenges and Risks

In fiscal 2016, we generated greater than 95% of our total revenues from contracts with the U.S. government and greater than 60% of our total revenues from contracts with the DoD, including subcontracts on which we perform. Our business performance is affected by the overall level of U.S. government spending (especially defense spending) and the alignment of our offerings and capabilities with the budget priorities of the U.S. government. While we believe that national security will continue to be a priority, the U.S. government budget deficit and the national debt have created pressure to examine and reduce spending across all federal agencies. Baseline spending for the DoD through U.S. government fiscal year 2023 has been reduced, and there may be further changes that negatively impact discretionary spending trends across all government agencies. Adverse changes in fiscal and economic conditions could materially impact our business. Some changes that could have an adverse impact on our business are the manner in which spending reductions are implemented (including sequestration), future government shutdowns, and issues related to required increases to the nation's debt ceiling.

The U.S. government has increasingly relied on contracts that are subject to a competitive bidding process (including indefinite delivery/indefinite quantity (IDIQ), U.S. General Services Administration (GSA) schedules and other multi-award contracts) which has resulted in greater competition and increased pricing pressure. We expect that a majority of the business that we seek in the foreseeable future will be awarded through a competitive bidding process.

Despite the budget and competitive pressures impacting the industry, we believe we are well positioned to protect and expand existing customer relationships and benefit from opportunities that we have not previously pursued. Our scale, size and prime contractor leadership position are expected to help differentiate us from our competitors, especially on large contracts. Our long-term, trusted customer relationships and deep technical expertise provide us with the sophistication to handle highly complex mission-critical contracts. SAIC's value proposition is found in the proven ability to serve as a trusted adviser to our customers. In doing so, we leverage our expertise and scale to help them execute their mission.

We succeed as a business based on the solutions we deliver, our past performance and our ability to compete on price. Our solutions, inspired through innovation, are based on best practices and technology transfer. Our past performance was achieved by employee dedication and customer focus. Our current cost structure, as well as our ongoing efforts to reduce costs by strategic sourcing and developing repeatable offerings, is expected to allow us to compete effectively on price in an evolving environment. Our ability to be competitive in the future will continue to be driven by our reputation of successful program execution, competitive cost structure and efficiencies in assigning the right people, at the right time, in support of our contracts.

The fiscal 2016 acquisition of Scitor Holdings, Inc. (Scitor) adds differentiated capabilities primarily in the classified work environment, and provides us access to significant portions of the intelligence community market that we did not have previously. Additionally, there is an opportunity to leverage our existing capabilities to provide expanded services to Scitor's customers.

See "Risk Factors" in Part I of this report for additional discussion of our industry and regulatory environment.

Management of Operating Performance and Reporting

We manage our business to achieve our long-term financial targets, which we expect to accomplish on average and over time. These financial targets include low single digit internal revenue growth, operating margin expansion of 10 to 20 basis points annually, and return of capital in excess of operating needs. Internal revenue growth (contraction) is the method by which we evaluate the growth generated by SAIC after acquisitions. We calculate internal revenue growth (contraction) by comparing our reported revenue for the current year to the reported revenue for the prior year comparable period adjusted to include the historical revenue of acquired businesses as if the acquisition took place in the comparable prior year period.

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Our business and program management process is directed by professional managers focused on satisfying our customers by providing high quality services in achieving contract requirements. These managers carefully monitor contract margin performance by constantly evaluating contract risks and opportunities. Through each contract's life cycle, program managers review performance and update contract performance estimates to reflect their understanding of the best information available. For contracts accounted for under the percentage-of-completion method in which incurred costs or efforts expended are used as a measure of progress to project completion, updates to estimates are recognized on inception-to-date activity, during the period of adjustment, resulting in either a favorable or unfavorable impact to operating income.

We evaluate our results of operations by considering the drivers causing changes in revenues, operating income and operating cash flows. Given that revenues fluctuate on our contract portfolio over time due to contract awards and completions, changes in customer requirements, and increases or decreases in ordering volume of materials, we evaluate significant trends and fluctuations in these terms. Whether performed by our employees or by our subcontractors, we primarily provide services on long-term contracts and, as a result, a significant portion of our cost of revenues fluctuates in concert with the changes in our revenues. We also analyze our revenues by type of cost (labor, subcontractor or materials) in order to understand operating margin because our labor-related revenues are generally more profitable. Changes in costs of revenues as a percentage of revenue other than from revenue volume or cost mix are normally driven by fluctuations in shared or corporate costs, changes in materials order volume, or cumulative revenue adjustments due to changes in contract estimates.

Changes in operating cash flows are described with regard to changes in cash generated through the delivery of services, significant drivers of fluctuations in assets or liabilities and the impacts of changes in timing of cash receipts or disbursements.

Results of Operations

The primary financial performance measures we use to manage our business and monitor results of operations are revenues, operating income and cash flows from operating activities. The following table summarizes our results of operations:

	Year Ended January 29, 2016	Percent change	January 30, 2015	Percent change	January 31, 2014
	(dollars in millions)				
Revenues	$4,284	12 %	$3,835	(5 %)	$4,017
Revenues performed by former Parent	31	(38 %)	50	(52 %)	104
Total revenues	4,315	11 %	3,885	(6 %)	4,121
Cost of revenues	3,873	11 %	3,500	(5 %)	3,684
Cost of revenues performed by former Parent	31	(38 %)	50	(52 %)	104
Total cost of revenues	3,904	10 %	3,550	(6 %)	3,788
Selling, general, and administrative expenses	158	66 %	95	3 %	92
Acquisition and integration costs	26	100 %	-	0 %	-
Separation transaction and restructuring expenses	-	0 %	-	(100 %)	58

Operating income	227	(5%)	240	31%	183
As a percentage of revenues	5.3%		6.3%		4.6%
As a percentage of revenues, excluding certain non-recurring costs (a)	5.9%		6.3%		6.0%
Net income	$117	(17%)	$141	25%	$113
Cash flows provided by operating activities	$226	(18%)	$277	51%	$183

(a) Operating income as a percentage of revenues excluding certain non-recurring costs (acquisition and integration costs associated with the acquisition of Scitor, and separation transaction and restructuring expenses that were incurred as a result of our separation from former Parent).

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Revenues. Revenues increased by $449 million, or 12%, from fiscal 2015 to 2016 primarily due to the acquisition of Scitor which contributed revenues of $428 million during fiscal 2016. The remainder of the increase is due primarily to revenue on newly awarded programs ($96 million) which was partially offset by decreased material volume ($60 million) and a DoD contract that ended in fiscal 2016 ($19 million).

Revenues decreased by $182 million, or 5%, from fiscal 2014 to 2015 as a result of the loss of the DISN Global Solutions program ($116 million), lower DoD subcontract and material revenues ($95 million), lower in-theater logistics activity ($60 million), and the completion of an Army Reserve and National Guard technical support program ($45 million). These decreases were partially offset by revenue on newly awarded programs ($91 million) and increased material volume on supply chain contracts ($64 million).

Revenues performed by former Parent decreased in fiscal 2015 and fiscal 2016 due to the expected ramp down of pre-separation joint work. These revenues are recorded equal to cost to reflect that no additional profit is charged to the customer for work performed by former Parent.

Cost of Revenues. We classify indirect costs incurred within or allocated to our U.S. government customers as cost of revenues or selling, general and administrative expenses (SG&A) in the same manner as such costs are defined in our Disclosure Statements that we prepare in accordance with CAS. We updated our Disclosure Statements effective in fiscal 2016, which resulted in certain types of costs that had previously been included in cost of revenues to be included in SG&A ($10 million for fiscal 2016); however, total operating costs were not affected by this change.

Cost of revenues increased by $373 million, or 11%, from fiscal 2015 to fiscal 2016 primarily driven by the acquisition of Scitor which contributed costs of $363 million during fiscal 2016. Costs of revenue as a percentage of revenue decreased from fiscal 2015 to fiscal 2016 due primarily to improved profitability across our contract portfolio. In addition, as described above, cost of revenues decreased, with a corresponding increase to SG&A, as a result of the update to our Disclosure Statements.

Cost of revenue decreased by $184 million, or 5%, from fiscal 2014 to fiscal 2015. Costs of revenue as a percentage of revenue decreased due primarily to net favorable changes in estimates on contracts accounted for under the percentage-of-completion method ($15 million).

Selling, General and Administrative Expenses. SG&A increased $63 million, or 66%, from fiscal 2015 to 2016 primarily due to additional amortization of intangible assets from the Scitor acquisition ($32 million) and other administrative costs attributable to Scitor's operations ($22 million). In addition, as described above, SG&A increased, with a corresponding decrease to cost of revenues, as a result of the update to our Disclosure Statements.

From fiscal 2014 to fiscal 2015 SG&A expenses were relatively consistent, with an increase of $3 million, or 3%.

Operating Income. Operating income decreased $13 million to 5.3% of revenues from fiscal 2015 to 2016 primarily due to acquisition and integration expenses related to the acquisition of Scitor ($26 million) which was partially offset by operating income generated by Scitor ($11 million after $32 million of amortization of intangible assets acquired) and a net favorable increase in the change in estimates on contracts accounted for under the percentage-of-completion method ($2 million).

Operating income increased $57 million to 6.3% of revenues from fiscal 2014 to 2015 primarily due to the absence of separation transaction and restructuring expenses in fiscal 2015 ($58 million) combined with strong program execution resulting in a net favorable increase in the change in estimates on contracts accounted for under the percentage-of-completion method ($15 million), both partially offset by lower revenue volume ($16 million).

Net Income. Net income decreased $24 million from fiscal 2015 to 2016 primarily due to increased interest expense on incremental term loan borrowings related to the Scitor acquisition ($17 million, net of tax) and decreased operating income ($8 million, net of tax) partially offset by a decrease in the effective tax rate ($1 million).

From fiscal 2014 to fiscal 2015 net income increased $28 million primarily due to the absence of separation transaction and restructuring costs in fiscal 2015 ($37 million, net of tax) which was partially offset by increased interest expense on term loan borrowings ($6 million, net of tax) and an increase in the effective tax rate ($2 million).

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Cash Flows Provided by Operating Activities. Cash flows provided by operating activities were $226 million for fiscal 2016 which represented a decrease from fiscal 2015 primarily due to the timing of income tax payments in the prior year ($29 million), current year payments for acquisition and integration costs ($18 million), an internal investment of working capital in the current year for the Assault Amphibious Vehicle contract ($29 million), and higher interest payments in the current year as a result of additional borrowings ($19 million). These decreases were partially offset by cash provided from the operating activities of Scitor.

From fiscal 2014 to fiscal 2015 cash flows provided by operating activities was $277 million, an increase of $94 million, or 51%. Cash flows increased from fiscal 2014 due to utilization of prepaid income taxes of $29 million, higher net income of $28 million and strong customer collections across several programs. Further contributing to the increase was the absence of payments to employees associated with a change in our vacation accrual policy that reduced cash flows provided by operating activities in fiscal 2014.

Non-GAAP Measures

Internal revenue growth (contraction), earnings before interest, taxes, depreciation and amortization (EBITDA), and adjusted EBITDA are non-GAAP financial measures that we reconcile to the most directly comparable GAAP financial measure. These measures are not meant to be considered in isolation or as a substitute for comparable GAAP measures and should be read only in conjunction with our consolidated and combined financial statements prepared in accordance with GAAP. The method that we use to calculate internal revenue growth (contraction), EBITDA, and adjusted EBITDA are not necessarily comparable to similarly titled financial measures presented by other companies.

Internal Revenue Growth (Contraction). We utilize internal revenue growth (contraction) to evaluate performance of our business post-acquisitions. We calculate internal revenue growth (contraction) by comparing our reported revenue for the current year to the reported revenue for the prior year comparable period adjusted to include the historical revenue of acquired businesses as if the acquisition took place in the comparable prior year period. This calculation has the effect of adding revenue for the acquired businesses for the comparable prior year to our prior year reported revenue. We believe internal revenue growth (contraction) percentage is useful to management and investors as an indicator of how successful we are at growing our base business and how successful we are at growing the revenues of the businesses that we acquire. The integration of acquired businesses allows our management to leverage business development capabilities, drive internal resource collaboration, utilize access to markets and qualifications, and refine strategies to realize synergies, which benefits both acquired and existing businesses. As a result, the performance of our business post-acquisition is an important measurement.

Internal revenue growth (contraction) for the current fiscal year was calculated as follows:

	Year Ended January 29, 2016 (in millions)
Prior year period's revenues, as reported	$ 3,835
Revenues of acquired business for the comparable prior year period	452
Prior year period's revenues, as adjusted	$ 4,287

Current year revenues, as reported	4,284	
Internal revenue contraction	$ (3	)
Internal revenue contraction, as a percentage	(0.1	%)

Internal revenue contraction for fiscal 2016 was $3 million, or less than 1%, when adjusting prior year revenues to include historical revenues for Scitor as if the acquisition occurred at the beginning of the comparable prior year period. Revenue generated by Scitor contracted $24 million due to delays in contract awards and transition of work to small business set aside contracts. This contraction was offset by net increases in revenue across other programs.

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EBITDA and Adjusted EBITDA. We utilize adjusted EBITDA to evaluate our performance by eliminating items that we do not consider to be indicative of our ongoing operating performance. We calculate adjusted EBITDA by calculating EBITDA and adjusting it by adding back the costs of acquiring and integrating Scitor. We believe EBITDA is a useful supplemental measure that helps investors better understand the operating performance and profitability trends of our business from period to period and provides useful information on how successfully we operate in our markets. We believe adjusted EBITDA is a useful supplemental measure that helps investors compare and evaluate our operating results from period to period without regard to the impact of items we do not consider indicative of ongoing operating performance due to their inherent unusual or non-recurring nature.

EBITDA and adjusted EBITDA for the current and prior fiscal years were calculated as follows:

	Year Ended		
	January 29, 2016	January 30, 2015	January 31, 2014
	(in millions)		
Net income	$117	$ 141	$ 113
Interest expense	44	17	7
Provision for income taxes	66	82	63
Depreciation and amortization	59	20	13
EBITDA	286	260	196
EBITDA as a percentage of revenues	6.7 %	6.8 %	4.9 %
Acquisition and integration costs	26	-	-
Depreciation included in acquisition and integration costs	(3)	-	-
Separation transaction and restructuring expenses	-	-	58
Adjusted EBITDA	$309	$ 260	$ 254
Adjusted EBITDA as a percentage of revenues	7.2 %	6.8 %	6.3 %

Fiscal 2016 adjusted EBITDA increased $49 million to 7.2% of revenues from 6.8% of revenues for the prior year due to the acquisition of Scitor, which has a relatively higher EBITDA margin percentage than our historical business, and a net increase in profitability across our existing contract portfolio. Fiscal 2015 adjusted EBITDA increased $6 million to 6.8% of revenues from 6.3% of revenues due to improved profitability in our contract portfolio.

Other Key Performance Measures

In addition to the financial measures described above, we believe that bookings and backlog are useful measures for management and investors to evaluate our potential future revenues. We also consider measures such as contract types and revenue mix to be useful for management and investors to evaluate our operating income and performance.

Bookings and Backlog. We had net bookings worth an estimated $4.3 billion and $3.4 billion during fiscal 2016 and fiscal 2015, respectively. Fiscal 2016 total backlog has increased from the prior year primarily due to the acquisition of Scitor during the second quarter. $1.1 billion of backlog from Scitor was recorded as an increase to our backlog as of the acquisition date.

Net bookings represent the estimated amount of revenue to be earned in the future from funded and negotiated unfunded contract awards that were received during the period, net of adjustments to estimates on previously awarded contracts. We calculate net bookings as the period's ending backlog plus the period's revenues less the prior period's ending backlog and initial backlog obtained through acquisitions. Scitor contract awards have been included in net bookings from the date of acquisition through January 29, 2016.

Backlog represents the estimated amount of future revenues to be recognized under negotiated contracts as work is performed. We do not include in backlog estimates of revenues to be derived from IDIQ contracts, but rather record backlog and bookings when task orders are awarded on these contracts. Given that much of our revenue is derived from IDIQ contract task orders that renew annually, bookings on these contracts tend to refresh annually as the task orders are renewed. Additionally, we do not include in backlog contract awards that are under protest until the protest is resolved in our favor. Bookings and backlog from contracts with government agencies fluctuate from period to period depending on a number of factors which include the government's initial procurement plans dictating the scope of required services and means of procuring them as well as the eventual timing and value of contract awards; subsequent task order renewals and contract modifications; and potential cancellations of existing work.

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We segregate our backlog into two categories as follows:

- Funded Backlog. Funded backlog for contracts with government agencies primarily represents estimated amounts of revenue to be earned in the future for which funding is appropriated less revenues previously recognized on these contracts. It does not include the unfunded portion of contracts for which funding is incrementally appropriated or authorized on a quarterly or annual basis by the U.S. government and other customers even though the contract may call for performance over a number of years. Funded backlog for contracts with non-government customers represents the estimated value on contracts, which may cover multiple future years, under which we are obligated to perform, less revenues previously recognized on these contracts.
- Negotiated Unfunded Backlog. Negotiated unfunded backlog represents estimated amounts of revenue to be earned in the future from negotiated contracts for which funding has not been appropriated or otherwise authorized and unexercised priced contract options. Negotiated unfunded backlog does not include any estimate of future potential task orders expected to be awarded under IDIQ, GSA Schedule or other master agreement contract vehicles.

We expect to recognize revenue from a substantial portion of our funded backlog within the next 12 months (from the end of the reporting period). However, the U.S. government can adjust the scope of services of or cancel contracts at any time. Similarly, certain contracts with commercial customers include provisions that allow the customer to cancel prior to contract completion. Most of our contracts have cancellation terms that would permit us to recover all or a portion of our incurred costs and fees (contract profit) for work performed.

The estimated value of our total backlog as of the dates presented was:

	January 29, 2016	January 30, 2015
	(in millions)	
Funded backlog	$1,879	$1,659
Negotiated unfunded backlog	5,319	4,513
Total backlog	$7,198	$6,172

Contract Types. Our earnings and profitability may vary materially depending on changes in the proportionate amount of revenues derived from each type of contract. For a discussion of the types of contracts under which we generate revenue, see “Business—Contract Types” in Part I of this report. The following table summarizes revenues by contract type as a percentage of total revenues for the periods presented:

	Year Ended January 29, 2016	January 30, 2015	January 31, 2014
Cost reimbursement	39 %	37 %	37 %
Time and materials (T&M)	29 %	29 %	31 %
Firm-fixed price (FFP)	32 %	34 %	32 %
Total	100 %	100 %	100 %

The contract portfolio acquired from Scitor consists of a higher proportion of cost reimbursable contracts, and a lower proportion of FFP contracts, than our historical contract portfolio.

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Revenue Mix. We generate revenues under our contracts from the efforts of our employees (which we refer to below as labor-related revenues), the efforts of our subcontractors and the materials provided on a contract. Revenues generated from supply chain materials entail the provision of tailored logistics support. Our subcontractor, contract materials, and supply chain materials revenues generally have lower margins than our labor-related revenues. The following table presents changes in labor-related, subcontractor-related and materials-related revenues for the periods presented:

	Year Ended January 29, 2016	Percent change	January 30, 2015	Percent change	January 31, 2014
	(dollars in millions)				
Labor-related revenues	$2,009	16 %	$1,738	(3 %)	$1,785
As a % of total revenues	47 %		45 %		43 %
Subcontractor-related revenues	1,460	16 %	1,255	(17 %)	1,507
As a % of total revenues	34 %		32 %		37 %
Supply chain materials-related revenues	613	0 %	616	8 %	573
As a % of total revenues	14 %		16 %		14 %
Other materials-related revenues	233	(16 %)	276	8 %	256
As a % of total revenues	5 %		7 %		6 %

Labor and subcontractor-related revenues increased and supply-chain and other materials-related revenues decreased as a percentage of total revenues in fiscal 2016 relative to fiscal 2015 primarily due to the Scitor acquisition because Scitor’s revenues are substantially generated through labor and subcontractors. Additionally, other materials-related revenues decreased in fiscal 2016 as a result of changes in order volume.

Labor-related revenues as a percentage of total revenues increased in fiscal 2015 relative to fiscal 2014 due to a relative decrease in subcontractor revenue and our continued efforts to adjust our contract labor mix in favor of work performed by our employees. Subcontractor-related revenues decreased in fiscal 2015, primarily due to funding delays on certain DoD contracts as well as the loss of DGS (which largely ended in fiscal 2014). Supply chain materials-related revenues increased as a result of stronger than usual ordering activity by the DoD near the end of the government fiscal year and continued into the fourth quarter of fiscal 2015.

Liquidity and Capital Resources

In managing our liquidity and capital resources we target maintaining an average minimum cash balance of $150 million while also managing our debt level. We intend to deploy excess capital above the target cash balance through dividends, share repurchases, debt prepayments and strategic acquisitions. We use various financial measures when we develop and update our disciplined cash deployment methodology, which include evaluating cash provided by operating activities, free cash flow and financial leverage. Our business generally requires minimal infrastructure investment because we are primarily a services provider. We expect to fund our ongoing working capital, commitments and any other discretionary investments with cash on hand, future operating cash flows and, if needed, borrowings under our $200 million Revolving Credit Facility.

In the second quarter of fiscal 2016, we completed the strategic acquisition of Scitor. We financed the acquisition with cash on hand and by incurring $670 million of additional secured debt. As a part of the acquisition financing, we converted our prior Credit Facility from an unsecured facility to a secured facility.

Borrowings under our Term Loan A Facility, Term Loan B Facility and, if used in the future, our Revolving Credit Facility incur interest at a variable rate. In accordance with our risk management objectives, we hold fixed interest rate swap agreements to hedge the variability in interest payment cash flows on a substantial portion of our outstanding variable rate debt. These instruments are used to hedge the variability in interest payment cash flows and are accounted for as cash flow hedges. Under the swap agreements, we pay the fixed rate and the counterparties to the agreement pay a floating interest rate.

Our Credit Facility contains customary terms and conditions including financial covenants and covenants restricting the Company's ability to merge or consolidate with another entity or undertake other fundamental changes, enter into property sale and leaseback transactions, and incur liens. The Company’s dividends and share repurchases are limited under certain leverage ratios, and we may be required to make an annual debt prepayment (calculated as a portion of our excess cash flow as defined in the Second Amended Credit Agreement). See Note 10 of the notes to the consolidated and combined financial statements for a more complete understanding of our Credit Facility.

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During fiscal 2016 we repurchased approximately 1.1 million shares of our common stock for $50 million from the open market in connection with our existing share repurchase program. During fiscal 2015 we repurchased approximately 3.2 million shares for $139 million, bringing the total since the program's inception in December of 2013 to 4.7 million shares or $200 million.

We anticipate that our future cash needs will be for working capital, capital expenditures, and contractual and other commitments. When our cash generation enables us to exceed our target cash balance, we will deploy excess cash through dividends, share repurchases, debt prepayments or strategic acquisitions. Our ability to fund these needs will depend, in part, on our ability to generate cash in the future, which depends on our future financial results. Our future results are subject to general economic, financial, competitive, legislative and regulatory factors that may be outside of our direct control. Although we believe that the financing arrangements in place will permit us to finance our operations on acceptable terms and conditions for at least the next year, our future access to, and the availability of financing on acceptable terms and conditions will be impacted by many factors (including our credit rating, capital market liquidity and overall economic conditions). Therefore, we cannot ensure that such financing will be available to us on acceptable terms or that such financing will be available at all. Nevertheless, we believe that our existing cash on hand, generation of future operating cash flows, and access to bank financing and capital markets will provide adequate resources to fund our short-term liquidity and long-term capital needs.

Historical Cash Flow Trends

The following table summarizes our cash flows:

	Year Ended		
	January 29, 2016	January 30, 2015	January 31, 2014
	(in millions)		
Total cash flows provided by operating activities	$226	$ 277	$ 183
Total cash flows used in investing activities	(798)	(22)	(16)
Total cash flows provided by (used in) financing activities	466	(208)	86
Total (decrease) increase in cash and cash equivalents	$(106)	$ 47	$ 253

Cash Provided by Operating Activities. Refer to “Results of Operations” above for a discussion of the changes in cash provided by operating activities between fiscal 2016 and fiscal 2015 and between fiscal 2015 and fiscal 2014.

Cash Used in Investing Activities. Cash used in investing activities increased in fiscal 2016 due to the acquisition of Scitor.

Cash used in investing activities increased in fiscal 2015 primarily due to investments in the infrastructure necessary to operate as a stand-alone company after the separation from former Parent.

Cash Provided by/Used in Financing Activities. Cash provided by financing activities increased in fiscal 2016 primarily due to proceeds from borrowings obtained to fund the Scitor acquisition and lower share repurchase activity in the current year under our publicly announced repurchase program. These changes were partially offset by current year payments of deferred financing costs, related to the additional borrowings, and term loan principal payments.

Cash used in financing activities for fiscal 2015 increased compared to fiscal 2014. Fiscal 2014 cash flows provided by financing activities reflect proceeds from our $500 million term loan, partially offset by net transfers to former Parent of $103 million for pre-separation cash settlement activity as well as a $295 million dividend to former Parent in connection with the separation. Fiscal 2015 cash flows used in financing activities reflects four quarters of dividend payments compared to two quarters in the prior year as well as stock repurchases and principal payments on borrowings in the current year, which we did not engage in prior to separation from former Parent.

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Off-Balance Sheet Arrangements

For an understanding of our obligations relating to surety bonds, see Note 15 of the notes to the consolidated and combined financial statements contained within this report. For an understanding of our operating leases, see "Contractual Obligations" within this section and Note 13 of the notes to the consolidated and combined financial statements contained within this report.

Contractual Obligations

The following table summarizes, as of January 29, 2016, our obligations to make future payments pursuant to certain contracts or arrangements and provides an estimate of the fiscal years in which these obligations are expected to be satisfied:

	Payments Due by Fiscal Year				
	Total	2017	2018 - 2019	2020 - 2021	2022 - Thereafter
	(in millions)				
Contractual obligations:					
Long-term debt including current portion (1)	$1,087	$57	$498	$ 1	$ 531
Interest payments on long-term debt (2)	149	39	73	37	-
Operating lease obligations	189	48	73	48	20
Estimated purchase obligations (3)	56	41	12	3	-
Other long-term liabilities (4)	33	3	13	9	8
Total contractual obligations	$1,514	$188	$669	$ 98	$ 559

(1) The amounts presented are based on an anticipated loan repayment schedule. However, we may be required to make certain mandatory prepayments based on our level of cash flow generation and we also have the option to prepay loan principal amounts at any time.

(2) Amounts represent an estimate of future variable interest payments on the Term Loan Facilities based on scheduled outstanding principal amounts, current applicable margin and projected 1- and 3-month LIBOR as of January 29, 2016. In addition, the above table excludes the impact of Excess Cash Flow (as defined in the Second Amended and Restated Credit Agreement) payments on the Term Loan B facility and excludes the effects of interest rate swaps used to hedge against changes in 1- and 3-month LIBOR.

(3) Includes estimated obligations to transfer funds under legally enforceable agreements for fixed or minimum amounts or quantities of goods or services at fixed or minimum prices. Excludes purchase orders for services or products to be delivered pursuant to U.S. government contracts in which we have full recourse under normal contract termination clauses.

(4) Other long-term liabilities primarily consist of liabilities associated with deferred compensation plan obligations and deferred rent. Deferred compensation plan obligations have been allocated to fiscal years based on participants' payment elections on retirement and estimated retirement ages, but is subject to acceleration on participants' termination of employment prior to retirement. Deferred rent has been allocated to fiscal years on a straight-line basis over the remaining contractual lease term but actual expense may be accelerated on early termination of the lease arrangement (or vacating a leased facility prior to the end of the lease).

Commitments and Contingencies

We are subject to a number of reviews, investigations, claims, lawsuits and other uncertainties related to our business. For a discussion of these items, see Note 15 of the notes to the consolidated and combined financial statements contained within this report.

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Critical Accounting Policies

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated and combined financial statements, which are prepared in accordance with U.S. generally accepted accounting principles. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingencies, as well as the reported amounts of revenues, expenses, gains and losses during the reporting periods. Management evaluates these estimates and assumptions on an ongoing basis. Our estimates and assumptions have been prepared on the basis of the most current reasonably available information and, in some cases, are our basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Estimates and assumptions may change in the future as more current information is available.

Management believes that our critical accounting policies are those that are both material to the presentation of our financial condition and results of operations and require management's most difficult, subjective and complex judgments. Typically, the circumstances that make these judgments difficult, subjective and complex have to do with making estimates about the effect of matters that are inherently uncertain.

These policies are described below.

Revenue Recognition. We generate our revenues primarily from long-term contracts in which we provide technical, engineering and enterprise IT services directly for the U.S. government and as a subcontractor with other contractors engaged in work for the U.S. government. We evaluate the nature of the contract and the services provided when determining the accounting method utilized for each contract. We recognize a significant portion of our revenues using the cost-to-cost percentage-of-completion method of accounting which requires us to rely on the skill and expertise of our engineers, program managers and business management professionals in the many areas of cost estimation. These estimates of costs can span several years and take into account many factors which include the availability, productivity and cost of labor, potential delays in our performance and the level of future indirect cost allocations.

We provide for anticipated losses on all types of contracts by recording an expense in the amount of the total expected contract loss during the period when the loss is determined. Amounts billed and collected but not yet earned as revenues under certain types of contracts are deferred. Contract costs incurred for U.S. government contracts (including allocated indirect costs) are subject to audit and adjustment through negotiations with government representatives. Revenues on U.S. government contracts have been recorded in amounts that are expected to be realized on final settlement.

Changes in Estimates on Contracts. Changes in estimates of revenues, cost of revenues, or profits related to contracts accounted for using the percentage-of-completion method of accounting in which incurred costs or efforts expended are used to measure contract progress are recognized in the period in which such changes are made for the inception-to-date effect of the changes. If it is determined that a loss will result from the performance of a contract, the entire amount of the estimable future loss is charged against income in the period the loss is identifiable. Changes in these estimates can routinely occur during contract performance for a variety of reasons which include: changes in contract scope; changes in contract cost estimates due to unanticipated cost growth or retirements of risk for amounts different than estimated; changes in estimated incentive or award fees; and performance being better or worse than previously estimated. Aggregate changes in contract estimates increased operating income by $13 million for fiscal 2016, increased operating income by $11 million for fiscal 2015 and decreased operating income by $4 million for fiscal 2014. For additional information related to changes in estimates on contracts, including gross favorable and unfavorable adjustments as well as the impact to earnings per share, see Note 1 of the notes to the consolidated and combined financial statements contained within this report.

Business Combinations. We record all tangible and intangible assets acquired and liabilities assumed in a business combination at fair value as of the acquisition date, which is determined using a cost, market or income approach. The excess amount of the aggregated purchase consideration paid over the fair value of the net of assets acquired and liabilities assumed is recorded as goodwill. Acquisition date fair value represents the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants as measured on the acquisition date.

The valuations are based on information that existed as of the acquisition date. During the measurement period that shall not exceed one year from the acquisition date, we may adjust provisional amounts recorded for assets acquired and liabilities assumed to reflect new information that we have subsequently obtained regarding facts and circumstances that existed as of the acquisition date.

Acquisition-related costs that are not part of the purchase price consideration are expensed as incurred. These costs typically include transaction-related costs, such as finder's fees, and legal, accounting and other professional costs.

Goodwill and Intangible Assets. Goodwill is recorded as the difference between the aggregate consideration paid for an acquisition and the fair value of the net tangible and intangible assets acquired and liabilities assumed. Goodwill is not amortized, but rather tested for potential impairment annually at the beginning of the fourth quarter, or whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

The goodwill impairment test is a two-step process performed at the reporting unit level. Under the first step, we estimate and compare the fair value of each reporting unit to its respective carrying value including goodwill. If the fair value is less than the carrying value, a second step is performed to calculate the amount of impairment expense, which is equal to the difference between the reporting unit's carrying amount of goodwill and its implied fair value of goodwill. The implied fair value of the reporting unit's goodwill is the residual fair value derived by deducting the fair value of a reporting unit's identifiable assets and liabilities, excluding goodwill, from the fair value of the reporting unit calculated in the first step.

Determining the fair value of each reporting unit involves judgment and the use of estimates and assumptions. We estimate the fair value of our reporting units using either a market approach, income approach, or a combination of both. We reconcile the aggregate fair value of all of our reporting units our market capitalization as of the measurement date.

Under the income approach, we estimate the fair value of a reporting unit using a multi-year discounted cash flow model that involves assumptions about projected future revenue growth, operating margins, income tax rates, capital expenditures, discount rate and terminal value. The discount rate is an estimate of the cost of capital that a market participant would expect for the respective reporting unit. The terminal value represents the present value in the last year of the projection period of all subsequent cash flows into perpetuity.

Under the market approach, we estimate the fair value of a reporting unit based on multiples of earnings derived from observable market data of comparable public companies. We evaluate companies within our industry that have operations with observable and comparable economic characteristics and are similar in nature, scope and size to the reporting unit being compared. We analyze historical acquisitions in our industry to estimate a control premium that we incorporate into the fair value estimate of a reporting unit under the market approach.

In addition, determining the carrying value of each reporting unit requires judgment and involves the assignment of assets and liabilities to the reporting units based on a systematic and rational allocation methodology. Certain assets and liabilities may be specifically identified and assigned to a reporting unit based on the information contained within our financial systems; whereas, other assets and liabilities may be allocated using measurable relationships or other basis for allocation.

With the completion of the Scitor acquisition in May 2015, we established a new reporting unit primarily consisting of a majority of the former Scitor business. This reporting unit has a goodwill balance of $479 million. During the fourth quarter of fiscal 2016, we completed our annual goodwill impairment testing and determined that the excess (or “cushion”) of fair value over the carrying value for this new reporting unit was approximately 4%, or $30 million. Given the proximity of the impairment testing date to the date of acquisition, a significant cushion was not expected for this new reporting unit. However, if future operating results are lower than anticipated or there are increases in market participant cost of capital, a reduction in, or elimination of, the cushion and potential impairment charges could result. There was significant cushion associated with the Company’s other reporting units as of the fourth quarter fiscal 2016 annual goodwill impairment test date.

Intangible assets with finite lives are amortized using the method that best reflects how their economic benefits are utilized or, if a pattern of economic benefits cannot be reliably determined, on a straight-line basis over their estimated useful lives. Intangible assets with finite lives are assessed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

Income Taxes. Our income tax expense, deferred tax assets and liabilities, and liabilities for unrecognized tax benefits reflect our best estimate of current and future taxes to be paid and includes judgments related to matters for which ultimate resolution may not become known until the final resolution of an examination by taxing authorities.

We record net deferred tax assets to the extent we believe these assets will more likely than not be realized. In making this determination, we consider all available positive and negative evidence, including future reversals of existing taxable temporary differences, projected future taxable income, tax planning strategies and recent operating results. If we were to determine that we would be able to realize our deferred income tax assets in the future in excess of their net recorded amount or would no longer be able to realize our deferred income tax assets in the future as currently recorded, we would make an adjustment to the valuation allowance which would either decrease or increase, respectively, the provision for income taxes.

We also recognize liabilities for uncertainty in income taxes when it is more likely than not that a tax position will not be sustained on examination and settlement with various taxing authorities. Liabilities for any uncertainty in income taxes are measured based on our estimate of the largest amount of benefit that is greater than 50% likely of being realized on ultimate settlement.

Stock-Based Compensation. We issue stock-based awards, including stock options, vesting stock awards and performance share awards as compensation to employees and directors. These awards are accounted for as equity awards. We recognize stock-based compensation expense net of estimated forfeitures on a straight-line basis over the underlying award's requisite service period, as measured using the award's grant date fair value. For performance share awards, we reassess the probability of achieving the performance conditions at each reporting period and adjusts compensation expense based on the number of shares we expect to ultimately issue. Absent sufficient history as a stand-alone company, we estimate forfeitures using former Parent's historical experience.

We use the Black-Scholes option-pricing model to calculate the grant date fair value of stock options awarded. The model calculates the fair value based on input assumptions about, among other things, employee exercise behavior and the expected volatility of our common stock. The assumptions used in the model represent our best estimates, but these estimates involve inherent uncertainties and the application of judgment. As a result, if factors change and we use different assumptions, our stock-based compensation expense could be materially different in the future. In addition, we are required to estimate the expected forfeiture rate and recognize expense only for those awards expected to vest. If our actual forfeiture rate is materially different from our estimate, the stock-based compensation expense could be significantly different from what we have recorded over the awards' respective service periods. For further discussion on the assumptions used, see Note 7 of the notes to the consolidated and combined financial statements contained within this report.

Recently Issued But Not Yet Adopted Accounting Pronouncements

For information on recently issued but not yet adopted accounting pronouncements, see Note 1 of the notes to the consolidated and combined financial statements contained within this report.

Effects of Inflation

For any of the most recent three fiscal years ended January 29, 2016, inflation has not had a significant impact on revenues or costs. Most of our contracts are paid in U.S. dollars and our cost to perform on these contracts are generally paid in U.S. dollars, so inflation risk is generally limited to that which is related to the U.S. dollar. Approximately 39% of our revenues for fiscal 2016 were derived from cost-reimbursement type contracts, which have limited inflation risk because our contracts generally entail the provision of labor on a reimbursable basis, and, when materials are acquired, they provide for billing to the customer during the period in which the materials were received. Bids for longer-term FFP and T&M contracts typically include sufficient provisions for labor and other cost escalations to cover anticipated cost increases over the period of performance. As a result, if we were to experience significant levels of inflation, our revenues and costs for cost-type contracts would generally both increase commensurate with inflation and operating income as a percentage of total revenues would not be significantly affected. Operating income as a percentage of total revenues would not be significantly affected for longer-term FFP and T&M contracts to the extent that bid contract cost escalations are sufficient to cover heightened inflation levels.

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Item 7A. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to certain market risks in the normal course of business. The following information about our market sensitive financial instruments contains forward-looking statements.

Foreign Currency Risk

Since the substantial majority of our business is conducted in U.S. dollars, a 10% change in any foreign currency exchange rates would not have a material impact to our financial condition or r