

Stanley, Inc.
Form 10-Q
October 29, 2009
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x

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

For the quarterly period ended September 25, 2009

OR

o

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

Commission File No. 001-33083

STANLEY, INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

3101 Wilson Boulevard, Suite 700

Arlington, VA

(Address of principal executive offices)

11-3658790

(I.R.S. Employer
Identification No.)

22201

(Zip Code)

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(703) 684-1125

(Registrant's telephone number,
including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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

- | | |
|-------------------------------------------------------------------------------------------------|-------------------------------------------------------|
| <input type="checkbox"/> Large accelerated filer | <input checked="" type="checkbox"/> Accelerated filer |
| <input type="checkbox"/> Non-accelerated filer
(do not check if a smaller reporting company) | <input type="checkbox"/> Smaller reporting company |

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

As of October 26, 2009, there were 24,046,144 shares of our Common Stock, par value \$0.01 per share, outstanding.

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STANLEY, INC.

FORM 10-Q

FOR THE QUARTER ENDED SEPTEMBER 25, 2009

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FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements include, in particular, statements about our plans, strategies and prospects. Forward-looking statements are generally identifiable by use of forward-looking terminology such as may, will, should, potential, intend, expect, endeavor, seek, estimate, overestimate, underestimate, believe, could, project, predict, continue or other similar words or expressions. References to the Company refer to Stanley, Inc., together in each case with our consolidated subsidiaries unless the context suggests otherwise.

The forward-looking statements contained in this Quarterly Report on Form 10-Q are based on current expectations, estimates, forecasts and projections about the industry in which we operate and management's beliefs and assumptions. These statements are not guarantees of future performance and involve risks, uncertainties and assumptions that are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements, including as a result of risks discussed in Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the fiscal year ended March 31, 2009. These forward-looking statements include, but are not limited to, statements relating to:

- our ability to retain customers and contracts, as well as our ability to win new customers and engagements;
- our backlog;
- risks associated with the acquisition and integration of new companies;
- our beliefs about trends in our market, available government contracts and outsourcing to companies like ours;
- expected spending on information technology and other professional services by federal government agencies, including the Department of Defense; and
- other risks discussed in our Annual Report on Form 10-K for the fiscal year ended March 31, 2009, in the sections entitled Risk Factors and Management's Discussion and Analysis of Financial Condition and Results of Operations, and in any other documents we file with the Securities and Exchange Commission.

We are under no duty to update any of the forward-looking statements after the date of this Quarterly Report on Form 10-Q to conform these statements to actual results, except as required by law.

Table of Contents**PART I: FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****STANLEY, INC. AND SUBSIDIARIES****Condensed Consolidated Statements of Income****(unaudited)****(in thousands, except per share data)**

	Three Months Ended		Six Months Ended	
	September 25, 2009	September 26, 2008	September 25, 2009	September 26, 2008
Revenues	\$ 217,089	\$ 191,078	\$ 425,835	\$ 363,645
Operating costs and expenses:				
Cost of revenues	180,518	159,925	353,607	305,684
Selling, general and administrative	13,401	12,224	27,492	22,883
Depreciation and amortization	2,852	2,586	5,682	4,428
Total operating costs and expenses	196,771	174,735	386,781	332,995
Operating income	20,318	16,343	39,054	30,650
Other income (expense):				
Other income		1	3	3
Interest income	21	71	59	196
Interest expense	(897)	(1,830)	(2,045)	(2,367)
Total other expenses	(876)	(1,758)	(1,983)	(2,168)
Income before taxes	19,442	14,585	37,071	28,482
Provision for income taxes	(7,689)	(5,857)	(14,654)	(11,437)
Net income	\$ 11,753	\$ 8,728	\$ 22,417	\$ 17,045
Earnings per share:				
Basic	0.50	\$ 0.38	\$ 0.96	\$ 0.75
Diluted	\$ 0.49	\$ 0.37	\$ 0.93	\$ 0.72
Weighted-average shares:				
Basic	23,447	22,793	23,364	22,760
Diluted	24,058	23,817	24,018	23,763

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

Table of Contents**STANLEY, INC. AND SUBSIDIARIES****Condensed Consolidated Balance Sheets****(unaudited)****(in thousands, except share data)**

	September 26, 2009	March 31, 2009
Assets		
Current assets:		
Cash	\$ 8,272	\$ 1,811
Accounts receivable - net	179,167	187,680
Prepaid and other current assets	8,040	6,766
Total current assets	195,479	196,257
Property and equipment - net	19,506	19,552
Goodwill	262,705	262,705
Intangible assets - net	12,600	15,557
Deferred taxes	4,285	4,212
Other assets	4,246	3,269
Total assets	\$ 498,821	\$ 501,552
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$ 19,707	\$ 21,528
Accrued expenses and other liabilities	72,289	79,841
Current portion of long-term debt	1,000	1,000
Income taxes payable		2,034
Total current liabilities	92,996	104,403
Line of credit	113,700	135,030
Long-term debt - net of current portion	34,250	34,500
Other long-term liabilities	10,086	10,396
Total liabilities	251,032	284,329
Commitments and contingencies		
Stockholders' equity:		
Common stock, \$0.01 par value - 200,000,000 shares authorized; 24,025,689 and 23,813,334 issued, respectively	240	238
Additional paid-in capital	104,999	96,957
Retained earnings	143,851	121,434
Accumulated other comprehensive loss	(906)	(886)
Deferred compensation	(395)	(520)
Total stockholders' equity	247,789	217,223
Total liabilities and stockholders' equity	\$ 498,821	\$ 501,552

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

Table of Contents**STANLEY, INC. AND SUBSIDIARIES****Condensed Consolidated Statements of Cash Flows**

(unaudited)

(in thousands)

	Six months ended	
	September 25, 2009	September 26, 2008
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 22,417	\$ 17,045
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	5,682	4,428
Loss on disposal of property and equipment	65	137
Deferred taxes	(389)	98
Stock contributed to employee stock ownership plan	812	
Income tax benefit from stock-based compensation	1,564	2,201
Stock compensation expense	3,486	2,789
Changes in assets and liabilities net of acquisition effects:		
Accounts receivable	8,513	18,474
Prepaid expenses and other current assets	(1,274)	612
Other assets	(977)	(357)
Accounts payable	(1,821)	(4,205)
Accrued expenses	(7,718)	(6,301)
Other liabilities	282	4,399
Income taxes payable	(2,035)	(6,102)
Net cash provided by operating activities	28,607	33,218
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of Oberon net of cash acquired		(167,824)
Acquisition of property and equipment	(2,601)	(5,050)
Net cash used in investing activities	(2,601)	(172,874)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net (repayments) borrowings under line-of-credit agreements	(21,330)	152,207
Repayment of long term debt	(250)	(250)
Payments under capital lease obligations	(146)	(145)
Purchase of treasury stock	(84)	(196)
Proceeds from exercise of stock options	1,574	795
Excess tax benefit from share-based compensation	410	505
Proceeds from the sale of stock	281	
Net cash (used in) provided by financing activities	(19,545)	152,916
NET INCREASE IN CASH	6,461	13,260
CASH Beginning of period	1,811	271
CASH End of period	\$ 8,272	\$ 13,531
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the period for:		
Income taxes	\$ 18,265	\$ 13,328
Interest	\$ 1,691	\$ 1,736

SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING

ACTIVITIES:

Lease incentive	\$	\$	942
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The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of Contents**STANLEY, INC. AND SUBSIDIARIES****Condensed Consolidated Statements of Comprehensive Income****(unaudited)****(in thousands)**

	Three Months Ended		Six Months Ended	
	September 25,	September 26,	September 25,	September 26,
	2009	2008	2009	2008
Net income	\$ 11,753	\$ 8,728	\$ 22,417	\$ 17,045
Other comprehensive income:				
Unrealized (loss) gain on interest rate swap	(12)	(44)	120	358
Translation adjustments	(74)	(6)	(140)	154
Total other comprehensive income	(86)	(50)	(20)	512
Comprehensive income	\$ 11,667	\$ 8,678	\$ 22,397	\$ 17,557

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

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STANLEY, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(unaudited)

(in thousands, except share and per share data, or as otherwise noted)

1. DESCRIPTION OF BUSINESS

Stanley, Inc., together with its subsidiaries (Stanley or the Company), is a provider of information technology services and solutions to U.S. defense, intelligence and federal civilian government agencies. Stanley offers its customers solutions to support any stage of program, product development or business lifecycle through five service areas: systems engineering, enterprise integration, operational logistics, business process outsourcing and advanced engineering and technology. The Company derives substantially all of its revenue from U.S. federal government agencies.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles (GAAP) in the United States and pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). In the opinion of management, these statements reflect all adjustments necessary to fairly present the Company's financial position as of September 25, 2009, and its results of operations and its cash flows for the six months ended September 25, 2009 and September 26, 2008. Certain information and note disclosures normally included in the annual financial statements have been condensed or omitted. The results of operations for the interim periods are not necessarily indicative of the results for the full year. For further information, refer to the financial statements and footnotes presented in the Company's Annual Report on Form 10-K for the fiscal year ended March 31, 2009.

Reporting Periods The Company's fiscal year begins on April 1 and ends on March 31. The Company's first three fiscal quarters end on the 13th Friday after the first day of the quarter and the fourth quarter ends on March 31. Fiscal quarters will typically be 13 weeks. The second quarter of fiscal year 2010 ended on September 25, 2009. The Company does not believe that there is a material impact to the comparability of the periods presented.

Principles of Consolidation The accompanying condensed consolidated financial statements include the accounts of Stanley's wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

Revenue Recognition The Company recognizes revenue under its contracts when a contract has been executed, the contract price is fixed and determinable, delivery of services or products has occurred, and collectibility is considered probable and can be reasonably estimated. Revenue is earned under cost-plus-fee, fixed-price and time-and-materials contracts. The Company uses a standard management process to determine whether all required criteria for revenue recognition have been met, which includes regular reviews of the Company's contract performance. This

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review covers, among other matters, progress against a schedule, outstanding action items, effort and staffing, quality, risks and issues, subcontract management, costs incurred, commitments, and customer satisfaction. During this review, the Company determines whether the overall progress on a contract is consistent with the effort expended.

Contract revenue recognition inherently involves the use of estimates. Examples of estimates include the contemplated level of effort to accomplish the tasks under the contract, the cost of the effort, and an ongoing assessment of the Company's progress toward completing the contract. From time to time, as part of the Company's standard management process, facts develop that require the Company to revise its estimated total costs and revenues. To the extent that a revised estimate affects contract profit or revenue previously recognized, the Company records the cumulative effect of the revision in the period in which the facts requiring the revision become known. The full amount of an anticipated loss on any type of contract is recognized in the period in which it becomes probable and can be reasonably estimated.

Under cost-plus-fee contracts, revenues are recognized as costs are incurred and include an estimate of applicable fees earned. For level of effort or term cost-plus-fee contracts, fixed fees are earned in proportion to the percentage of required effort delivered. The Company considers fixed fees under cost-plus-fee contracts to be earned in proportion to the allowable costs actually incurred in performance of the contract for level of effort contracts. For completion type cost-plus-fee contracts, fixed fees are earned in proportion to the percentage of work completed. For time-and-materials contracts, revenues are computed by multiplying the number of direct labor-hours expended in performance of the contract by the contractual billing rates and adding other billable direct and indirect costs. For fixed-price contracts, revenues are recognized as services are performed, using the percentage-of-completion method, applying the cost-to-cost or units of delivery method.

For cost-plus-award fee type contracts, the Company recognizes the expected fee to be awarded by the customer at the

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time such fee can be reasonably estimated, based on factors such as prior award experience and communications with the customer regarding performance, including any interim performance evaluations rendered by the customer. For cost-plus-incentive fee type contracts, the method of calculating the incentive fee is specified in the contract and it is typically based on measuring actual costs to perform the contract against a target cost to perform the contract. The Company prepares periodic estimates to complete the contract and adjusts the incentive fee as required based on the contract incentive fee formula.

The Company's contracts with agencies of the government are subject to periodic funding by the respective contracting agency. Funding for a contract may be provided in full at inception of the contract or ratably throughout the contract as the services are provided. From time to time, the Company may proceed with work based on customer direction prior to the completion and signing of formal contract documents. The Company has a formal internal review process and management approval prior to commencement of work. Revenue associated with such work is recognized without profit and only when it can be reliably estimated and realization is probable. The Company bases its estimates on notices to proceed from its customers, previous experiences with the customer, communications with the customer regarding funding status, and its knowledge of available funding for the contract or program. Pre-contract costs related to unsuccessful contract bids are expensed in the period in which we are notified that the contract will not be issued.

Disputes occasionally arise in the normal course of the Company's business due to events such as delays, changes in contract specifications, and questions of cost allowability or collectibility. Such matters, whether claims or unapproved change orders in the process of being negotiated, are recorded at the lesser of their estimated net realizable value or actual costs incurred, and only when realization is probable and can be reliably estimated. Claims against us are recognized where a loss is considered probable and can be reasonably estimated in amount.

The allowability of certain costs under government contracts is subject to audit by the government. Certain indirect costs are charged to contracts using provisional or estimated indirect rates, which are subject to later revision based on government audits of those costs. Management is of the opinion that costs subsequently disallowed, if any, would not be significant.

Concentration of Risk Contracts funded by federal government agencies account for substantially all of the Company's revenues. For the three months ended September 25, 2009 and September 26, 2008, the Company derived approximately 76% and 71% of its revenues, respectively, from the Department of Defense, including agencies within the intelligence community, and approximately 24% and 29% of its revenues, respectively, from federal civilian government agencies. The Company's contract with the Department of the Navy for production engineering and integration services under various Space and Naval Warfare Systems Command (SPAWAR) programs, which is its largest revenue-generating contract, accounted for approximately 11% of its revenues for the three months ended September 25, 2009.

For the six months ended September 25, 2009 and September 26, 2008, the Company derived approximately 75% and 67% of its revenues, respectively, from the Department of Defense, including agencies within the intelligence community, and approximately 25% and 33% of its revenues, respectively, from federal civilian government agencies. The Company's contract with the Department of the Navy for production engineering and integration services under various Space and Naval Warfare Systems Command (SPAWAR) programs, which is the largest revenue-generating contract, accounted for approximately 10% of its revenues for the six months ended September 25, 2009.

Property and Equipment Property and equipment are carried at cost, less accumulated depreciation. Depreciation of property and equipment is calculated using the straight-line method over the useful lives. The estimated useful lives of computers, peripherals and software typically range from three to five years. The estimated useful lives of furniture and equipment typically range from five to ten years. Leasehold improvements are amortized over the lesser of the useful life or the term of the lease. Repairs and maintenance are expensed as incurred. Depreciation expense related to property and equipment was \$1.3 million and \$1.0 million for the three months ended September 25, 2009 and September 26, 2008,

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respectively and \$2.6 million and 1.9 million for the six months ended September 25, 2009 and September 26, 2008, respectively.

Goodwill and Intangible Assets Goodwill represents the excess of cost over the fair value of net tangible and identifiable intangible assets of acquired companies. The Company does not amortize goodwill; rather it tests goodwill for impairment at least on an annual basis. Testing for impairment is a two-step process. The first step is a test for potential impairment, while the second step measures the amount of impairment, if any. The Company is required to perform an impairment test at least on an annual basis at any time during the fiscal year provided the test is performed at the same time every year. An impairment loss would be recognized when the assets' fair value is below their carrying value. Stanley has elected the last day of its third fiscal quarter as its testing date. Based on the testing performed as of December 26, 2008, the Company determined that no impairments existed. Intangible assets are amortized over their estimated useful lives. Customer relationships are amortized on a straight-line basis over periods ranging from five to seven years. Non-competition agreements are amortized on a straight-line basis over three years. Backlog and contracts are amortized on a straight-line basis over periods ranging from two to five years.

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Impairment of Long-Lived Assets Whenever events or changes in circumstances indicate that the carrying amount of long-lived assets may not be fully recoverable, Stanley evaluates the probability that future undiscounted net cash flows, without interest charges, will be less than the carrying amount of the assets. If any impairment were indicated as a result of this review, Stanley would recognize a loss based on the amount by which the carrying amount exceeds the estimated fair value. Management believes that no impairments existed as of September 25, 2009.

Earnings per share Basic earnings per share has been computed by dividing net income available to common stockholders by the weighted-average number of shares of common stock outstanding during each period. Restricted shares of common stock that vest based on the satisfaction of certain conditions are treated as contingently issuable shares until the conditions are satisfied. These shares are included in the computation of basic earnings per share only after the shares vest. Shares issued during the period and shares reacquired during the period are weighted for the portion of the period that they were outstanding. Diluted earnings per share consider the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. Shares that are anti-dilutive are not included in the computation of diluted earnings per share. The diluted weighted-average common shares outstanding for the three and six months ended September 25, 2009, exclude stock options to purchase approximately 0.1 million and 0.1 million shares, respectively, because such options have exercise prices in excess of the average market price of the Company's stock for that period. The weighted-average number of common shares outstanding is computed as follows:

	Three Months Ended		Six Months Ended	
	September 25, 2009	September 26, 2008	September 25, 2009	September 26, 2008
	(in thousands)			
Basic weighted-average common shares outstanding	23,447	22,793	23,364	22,760
Effect of stock options and unvested restricted stock grants	611	1,024	654	1,003
Diluted weighted-average common shares outstanding	24,058	23,817	24,018	23,763

Derivative Instruments and Hedging Activities Stanley entered into an interest rate swap agreement on October 27, 2006 with a maturity date of January 31, 2012, an annual fixed rate of 5.28% and a notional amount of \$19.0 million. The Company designated this swap agreement, at its inception, as a qualifying cash flow hedge. For qualifying cash flow hedges, the effective portion of derivative gains and losses are recorded as a component of other comprehensive income and are reclassified into earnings in the same period in which the hedged transaction affects such earnings. Any ineffectiveness is reported currently in earnings. The fair value of the hedge arrangement is recorded as an asset or a liability in the accompanying unaudited condensed consolidated balance sheets. The fair value of the swap at September 25, 2009 of \$1.5 million has been reported in *Accrued expenses and other liabilities* with an offset, net of tax, included in *Accumulated other comprehensive loss* in the accompanying unaudited condensed consolidated balance sheet. None of the \$1.5 million unrealized loss was recognized in earnings during the six months ended September 25, 2009 based on hedge ineffectiveness and none of the swap's unrealized loss was excluded from the assessment of hedge effectiveness. Amounts in accumulated other comprehensive loss will be reclassified into earnings in the period in which variable interest payments (the hedged transaction) are made under the Senior Credit Facility (defined in Note 6). Amounts paid or received on the swap are recorded as interest expense in the period incurred.

Segment Reporting Operating segments are defined as components of an enterprise for which separate financial information is available and evaluated regularly by the chief operating decision maker, or decision making group, in deciding how to allocate resources and assess performance. The Company currently has one reportable segment for financial reporting purposes, which represents the Company's core business of providing information technology solutions and services for federal government customers. The Company does not report revenue by product or service or groups of products or services because it is impracticable to do so.

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Use of Estimates The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant items subject to such estimates and assumptions include revenue recognition, carrying amount and useful lives of long-lived assets, valuation allowances for accounts receivable and deferred tax assets, software development costs and loss contingencies such as litigation, claims and assessments.

Reclassifications Certain reclassifications have been made to prior period balances to conform to the current presentation.

Subsequent Events The Company has evaluated subsequent events after the balance sheet date through the time of filing these financial statements with the SEC on October 29, 2009, for appropriate accounting and disclosure.

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Fair Value of Financial Instruments The fair value of accounts receivable, accounts payable, accrued expenses, debt, and the swap contract approximates their respective carrying amounts.

The three level fair value hierarchy to classify the inputs used in measuring fair value as follows:

Level 1: Quoted prices for identical instruments in active markets.

Level 2: Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-driven valuations whose inputs are observable or whose significant value drivers are observable.

Level 3: Significant inputs to the valuation model are unobservable.

As of September 25, 2009, the financial liability measured at fair value consisted of an interest rate swap agreement. The value is based on model-driven valuations whose inputs are observable. The following table summarizes the financial liability measured at fair value on a recurring basis as of September 25, 2009 and the level it falls within the fair value hierarchy:

	Fair Value Measurement Using:			Total September 25, 2009
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Liabilities:				
Interest rate swap	\$	\$ 1,506	\$	\$ 1,506

Recent Accounting Pronouncements In June 2009, the FASB issued Statement of Financial Accounting Standards No. 168, *The FASB Accounting Standards Codification* (Codification) and the *Hierarchy of Generally Accepted Accounting Principles* (GAAP), a replacement of *FASB Statement No. 162* (SFAS 168). SFAS 168 establishes the Codification as the single source of authoritative GAAP in the United States, other than rules and interpretive releases issued by the SEC. The Codification is a reorganization of current GAAP into a topical format that eliminates the current GAAP hierarchy and establishes instead two levels of guidance authoritative and nonauthoritative. All non-grandfathered, non-SEC accounting literature that is not included in the Codification will become nonauthoritative. The FASB's primary goal in developing the Codification is to simplify user access to all authoritative GAAP by providing all the authoritative literature related to a particular accounting topic in one place. The Codification was effective for interim and annual periods ending after September 15, 2009. Following SFAS 168, the Board will not issue new standards in the form of Statements, FASB Staff Positions, or Emerging Issue Task Force Abstracts; instead, it will issue Accounting Standards Updates. The FASB will not consider Accounting Standards Updates as authoritative in their own right; these updates will serve only to update the Codification, provide background information about the guidance, and provide the bases for conclusions on the change(s) in the Codification. In the description of Accounting Standards Updates that follows, references in italics relate to Codification Topics and Subtopics, and their descriptive titles, as appropriate.

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Accounting Standards Updates In June 2009, an update was made to *Consolidation - Consolidation of Variable Interest Entities*. Among other things, the update replaces the calculation for determining which entities, if any, have a controlling financial interest in a variable interest entity (VIE) from a quantitative based risks and rewards calculation, to a qualitative approach that focuses on identifying which entities have the power to direct the activities that most significantly impact the VIE's economic performance and the obligation to absorb losses of the VIE or the right to receive benefits from the VIE. The update also requires ongoing assessments as to whether an entity is the primary beneficiary of a VIE (previously, reconsideration was only required upon the occurrence of specific events), modifies the presentation of consolidated VIE assets and liabilities, and requires additional disclosures about a company's involvement in VIEs. This update will be effective for fiscal years beginning after November 15, 2009. The Company does not currently believe that the adoption of this update will have any effect on its consolidated financial position and results of operations.

In September 2009, an update was made to *Fair Value Measurements and Disclosures - Investments in Certain Entities that Calculate Net Asset Value per Share (or Its Equivalent)*. This update permits entities to measure the fair value of certain investments, including those with fair values that are not readily determinable, on the basis of the net asset value per share of the investment (or its equivalent) if such net asset value is calculated in a manner consistent with the measurement principles in *Financial Services-Investment Companies* as of the reporting entity's measurement date (measurement of all or substantially all of the underlying investments of the investee in accordance with the *Fair Value Measurements and Disclosures* guidance). The update also requires enhanced disclosures about the nature and risks of investments within its scope that are measured at fair value on a recurring or nonrecurring basis. This update will be effective for interim and annual periods ending after December 15, 2009. The

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Company is currently evaluating the effect that adoption of this update will have, if any, on its consolidated financial position and results of operations.

In October 2009, an update was made to *Revenue Recognition - Multiple Deliverable Revenue Arrangements*. This update removes the objective-and-reliable-evidence-of-fair-value criterion from the separation criteria used to determine whether an arrangement involving multiple deliverables contains more than one unit of accounting, replaces references to fair value with selling price to distinguish from the fair value measurements required under the *Fair Value Measurements and Disclosures* guidance, provides a hierarchy that entities must use to estimate the selling price, eliminates the use of the residual method for allocation, and expands the ongoing disclosure requirements. This update is effective for fiscal years beginning on or after June 15, 2010, and can be applied prospectively or retrospectively. The Company is currently evaluating the effect that adoption of this update will have, if any, on its consolidated financial position and results of operations.

3. ACCOUNTS RECEIVABLE

Accounts receivable consists of the following:

	As of September 25, 2009	As of March 31, 2009
Billed receivables	\$ 125,916	\$ 122,322
Unbilled receivables:		
Amounts billable	47,645	57,912
Revenues recorded in excess of contract funding	6,586	8,132
Retainage and contract fee withholding	360	451
Allowance for doubtful accounts	(1,340)	(1,137)
Total	\$ 179,167	\$ 187,680

Amounts billable consist primarily of amounts to be billed within a month. Revenues recorded in excess of contract funding are billable upon receipt of contractual amendments or modifications adding additional funding. The retainage and fee withholding is billable upon completion of the contract performance and approval of final indirect expense rates by the government. Consistent with industry practice, certain receivables related to long-term contracts are classified as current, although a portion of these amounts is not expected to be billed and collected within one year. Unbilled accounts receivable at September 25, 2009 are expected to be billed and collected within one year except for approximately \$0.4 million.

4. PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

As of September 25, 2009	As of March 31, 2009
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Computers and peripherals	\$	6,503	\$	5,684
Software		4,420		4,265
Furniture and equipment		6,309		5,669
Leasehold improvements		15,162		14,323
		32,394		29,941
Less: Accumulated depreciation and amortization		(12,888)		(10,389)
Property and equipment net	\$	19,506	\$	19,552
Property and equipment included above that are under capital lease obligations include:				
Software	\$	947	\$	947
Furniture and equipment		142		161
Less: Accumulated depreciation and amortization		(879)		(766)
Total	\$	210	\$	342

Table of Contents**5. ACCRUED EXPENSES AND OTHER LIABILITIES**

Accrued expenses and other liabilities consist of the following:

	As of September 25, 2009	As of March 31, 2009
Accrued payroll-related costs	\$ 21,425	\$ 28,089
Accrued contract costs	32,149	34,848
Accrued indirect costs	7,467	7,405
Other payables	11,248	9,499
Total accrued expenses	\$ 72,289	\$ 79,841

6. DEBT

The Company is party to credit agreement (Senior Credit Facility or Amended Credit Agreement) with a group of lenders for which SunTrust Robinson Humphrey, Inc. acted as sole book manager and lead arranger, SunTrust Bank acted as administrative agent and M&T Bank and BB&T Bank acted as co-documentation agents.

At September 25, 2009, the lenders aggregate commitment under the Senior Credit Facility was \$276.9 million, which consisted of a \$241.6 million revolving line of credit (Revolver) and a \$35.3 million term loan (Term Loan), and the Company had outstanding indebtedness of \$35.3 million on the Term Loan and \$113.7 million on the Revolver, with a weighted-average interest rate of approximately 1.70% and 3.75% for the six months ended September 25, 2009 and September 26, 2008, respectively. At September 25, 2009, the Company s borrowing availability under the Senior Credit Facility was \$127.9 million, including outstanding letters of credit.

Under the terms of the Amended Credit Agreement, the Company may request an increase in the size of the Revolver by an aggregate amount not greater than \$33.4 million. If any lender elects not to increase its commitment, the Company may designate another bank or other financial institution to become a party to the Amended Credit Agreement.

The Amended Credit Agreement also contains a number of affirmative and restrictive covenants, including limitations on mergers, consolidations and dissolutions; sales of assets; investments and acquisitions; indebtedness and liens; repurchases of shares of capital stock and options to purchase shares of capital stock; transactions with affiliates; sale and leaseback transactions; and restricted payments.

In addition, the Amended Credit Agreement requires the Company to meet the following financial covenants:

- a fixed charge coverage ratio as of the end of any fiscal quarter of not less than 1.35 to 1.00, based upon the ratio of (i) consolidated EBITDA (as defined in the Amended Credit Agreement) less the actual amount paid by the Company and its subsidiaries in cash on account of capital

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expenditures and taxes to (ii) consolidated interest expense for such period, scheduled principal payments required to be made on consolidated total debt during such period and certain restricted payments paid during such period, in each case measured for the four consecutive fiscal quarters ending on or immediately prior to such date; and

- a maximum leverage ratio not greater than 3.75 to 1.00, based upon the ratio of (i) consolidated total debt to (ii) consolidated EBITDA (as defined in the Amended Credit Agreement).

At September 25, 2009, the Company was in compliance with all covenants under its Senior Credit Facility. The obligations under the Senior Credit Facility are unconditionally guaranteed by each of Stanley's existing and subsequently acquired or organized subsidiaries and are secured on a first-priority basis by security interests (subject to permitted liens) in substantially all assets owned by the Company and each of its subsidiaries, including the shares of capital stock of its subsidiaries, subject to certain exceptions.

7. ACQUISITIONS

Oberon Associates, Inc.

On July 15, 2008, Stanley acquired Oberon Associates, Inc. (Oberon), an engineering, intelligence operations and information technology services company for approximately \$167.8 million at closing, net of cash acquired, plus an additional \$3.0 million in post closing net working capital and other purchase price adjustments. Stanley financed the acquisition with

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borrowings under its Senior Credit Facility.

Oberon provides engineering, operational intelligence and information technology support to multiple elements of the U.S. Army, in addition to the U.S. Air Force, Defense Information Systems Agency, Transportation Security Administration and several agencies throughout the intelligence community. Oberon's areas of expertise include biometrics systems engineering, integration and operational deployment; intelligence community support; communications engineering; and information technology and enterprise data management. The acquisition of Oberon expands the range of solutions offered to the Company's customers, bringing to Stanley biometric applications experts, functional experts within the intelligence community, and expertise in communications and information management systems.

The results of Oberon have been included in the accompanying condensed consolidated financial statements since the date of acquisition. The purchase price has been allocated to the assets acquired and liabilities assumed based upon their estimated fair values. Of the purchase consideration, \$149.1 million has been allocated to goodwill, based upon the excess of the purchase price over the \$8.6 million estimated fair value of net tangible assets and \$13.1 million has been assigned to other identifiable intangible assets. The Company completed its evaluation of the fair value of the assets and liabilities of Oberon and purchase accounting entries relating to the acquisition in the three months ended September 25, 2009. None of the amount allocated to goodwill is expected to be deductible for tax purposes. Included in identifiable intangibles arising from the Oberon acquisition are \$10.5 million, \$1.9 million and \$0.7 million related to customer contracts and relationships, order backlog and non-compete agreements, respectively. The amortization period for customer contracts and relationships, order backlog and non-compete agreements is five years, two years and three years, respectively. No residual value has been assumed at the end of their useful lives.

8. STOCKHOLDERS' EQUITY

Common Stock

Stanley has one class of common stock, with each share of common stock having one vote per share. Holders of common stock share in dividends declared, if any, by the board of directors.

Stanley repurchased 3,254 shares of stock from its employees for \$0.1 million during the six months ended September 25, 2009. The repurchases were made to satisfy certain employees' tax obligations upon the vesting of restricted stock. The shares were recorded at market price using the cost method of accounting.

Equity Compensation

Under the Amended and Restated 2006 Omnibus Incentive Compensation Plan (the "Omnibus Plan"), Stanley is authorized to provide awards for a maximum of 4,500,000 shares of common stock to directors, officers, employees or consultants. The Omnibus Plan allows for cash awards, restricted stock awards, restricted stock units, stock appreciation rights, performance units, fully vested shares, option awards and other equity-related awards. Vesting periods of these awards vary. Except as otherwise determined by the board of directors, the option awards may

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not have an exercise price less than the fair market value of the common stock on the date the option is granted.

Prior to July 2006, under the Executive Deferred Compensation and Equity Incentive Plan (the Executive Plan), Stanley was authorized to provide awards for a maximum of 15,000,000 shares of common stock to key employees and non-employee directors. The Executive Plan allowed for cash awards, restricted stock awards, restricted stock trust awards and option awards. Vesting periods of these awards varied. Holders of restricted stock awards have voting rights with respect to the awards. The trustee of restricted stock trust awards has voting rights with respect to the trust awards. The option awards granted under the Executive Plan have exercise prices that range from 85% to 110% of the fair market value of the common stock on the date the option was granted. No further grants under the Executive Plan will be made.

Effective April 1, 2006, the Company adopted the provisions of *Compensation Stock Compensation* using the prospective-transition method. Under that transition method, compensation cost recognized in the six months ended September 25, 2009 includes compensation cost for all share-based payments granted on or after April 1, 2006, based on the grant-date fair value. The Company is required to account for any portion of awards outstanding at the date of adoption of *Compensation Stock Compensation* using the accounting principles originally applied to those awards.

The Company has presented all tax benefits resulting from stock-based compensation awarded prior to the adoption of *Compensation Stock Compensation* as operating cash flows in the accompanying unaudited condensed consolidated statements of cash flows. The tax benefits associated with share-based compensation in effect prior to the adoption of *Compensation Stock Compensation* were \$1.6 million and \$2.2 million for the six months ended September 25, 2009 and September 26, 2008,

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respectively. For share-based payment transactions awarded subsequent to the adoption of SFAS No. 123(R), the tax benefits in excess of the compensation cost recognized are classified as financing cash flows. The excess tax benefits associated with share-based payment transactions accounted for after the adoption of *Compensation Stock Compensation* were \$0.4 million and \$0.5 million for the six months ended September 25, 2009 and September 26, 2008, respectively, and are disclosed within financing activities in the accompanying Condensed Consolidated Statements of Cash Flows.

The fair value of each option award is estimated on the date of grant using the Black-Scholes-Merton closed-form option-pricing model that uses the assumptions noted in the following table. Expected volatility for the six months ended September 25, 2009 was based on historical volatility of the Company's stock price. Expected volatility for the six months ended September 26, 2008 was based on a weighted-average of the historical volatilities of similar public entities. The expected term of options granted is derived using the simplified method and represents the period of time that options granted are expected to be outstanding. Options granted meet the criteria of "plain vanilla" for purposes of applying the simplified method. This method was used as the Company did not have sufficient historical exercise data to provide a reasonable basis upon which to estimate expected term due to the limited period of time the shares have been publicly traded. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant. The Company has not issued dividends in the past nor does it currently intend to issue dividends in the near future.

A summary of the weighted average assumptions is presented below.

	Six Months Ended	
	September 25, 2009	September 26, 2008
Expected volatility	38.8%	32.3%
Expected dividends	0.0%	0.0%
Expected term (in years)	3.5	3.5
Risk-free rate	1.6%	2.6%

During the six months ended September 25, 2009, the Company granted 457,976 stock option awards at a weighted-average exercise price of \$25.23, which reflects the fair value of the shares on the date of grant. These options vest ratably over three years and have a contractual term of five years. The weighted-average fair value of stock option awards granted during the six months ended September 25, 2009 and September 26, 2008, as determined by the Black-Scholes-Merton closed-form option-pricing model, was \$7.66 and \$7.22, respectively. The stock option awards that vested during the six months ended September 25, 2009 and September 26, 2008 had a combined fair value of \$2.1 million and \$1.2 million, respectively.

A summary of option activity for the year ended March 31, 2009, and the six months ended September 25, 2009 is presented below.

Options	Number of Underlying Shares	Weighted-Average Exercise Price	Aggregate Intrinsic Value (in thousands)
Outstanding at April 1, 2008	1,609,475	\$ 9.15	
Granted	445,210	\$ 26.43	
Exercised	(338,834)	\$ 5.17	\$ 7,762
Forfeited	(111,452)	\$ 14.90	
Outstanding at April 1, 2009	1,604,399	\$ 14.38	
Granted	457,976	\$ 25.23	
Exercised	(172,428)	\$ 9.13	\$ 3,492

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Forfeited	(56,480) \$	16.52	
Outstanding at September 25, 2009	1,833,467 \$	17.52 \$	16,538

A summary of nonvested stock option activity for the six months ended September 25, 2009 is presented below.

Nonvested Options	Number of Underlying Shares	Weighted-Average Fair Value	
Outstanding at April 1, 2009	1,051,141	\$	5.46
Granted	457,976	\$	7.66
Vested	(388,610)	\$	5.29
Forfeited	(56,250)	\$	5.33
Outstanding at September 25, 2009	1,064,257	\$	6.48

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A summary of vested stock options at September 25, 2009, and stock options expected to vest in future periods is presented below.

Options	Number of Underlying Shares	Weighted- Average Exercise Price	Weighted-Average Remaining Contractual Term (years)	Aggregate Intrinsic Value (in thousands)
Exercisable	769,210	\$ 12.29	3.9	\$ 10,963
Expected to vest	984,438	\$ 21.30	4.2	\$ 5,157
Exercisable and expected to vest	1,753,648			

During the six months ended September 25, 2009, the Company granted 61,121 restricted stock awards at a weighted-average fair value of \$26.01 per share that vest ratably over a period of three years. The weighted-average fair value of restricted stock awards granted during the six months ended September 25, 2009 and September 26, 2008 was \$26.01 and \$25.38, respectively. The restricted stock awards that vested during the six months ended September 25, 2009 and September 26, 2008 had a combined fair value of \$1.3 million and \$0.9 million, respectively.

A summary of restricted stock activity for the six months ended September 25, 2009 is presented below.

Restricted Stock	Number of Shares	Weighted-Average Fair Value
Outstanding at April 1, 2009	676,437	\$ 24.25
Granted	61,121	\$ 26.01
Vested	(62,337)	\$ 20.98
Forfeited	(56,940)	\$ 24.58
Outstanding at September 25, 2009	618,281	\$ 24.72

During the six months ended September 25, 2009 and September 26, 2008, the Company recognized \$3.5 million and \$2.8 million of share-based compensation costs, respectively. As of September 25, 2009, there was \$15.9 million of total unrecognized compensation cost related to nonvested share-based compensation arrangements granted under the Omnibus Plan. That cost is expected to be recognized over a weighted-average period of 2 years.

Prior to the adoption of *Compensation Stock Compensation*, the fair market value of each issuance and grant was determined by the Company on a contemporaneous basis. The Company recorded stock-based deferred compensation in aggregate of approximately \$1.4 million in connection with compensatory grants of stock options and shares of restricted stock awarded during fiscal 2006 and 2007. Approximately \$0.1 million of compensation expense was recognized during the six months ended September 25, 2009. The remaining deferred compensation of \$0.4 million will be amortized over the final 2 years of the vesting period of the awards.

9. COMMITMENTS AND CONTINGENCIES

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Contract Cost Audits Substantially all payments to Stanley under cost-reimbursable contracts and subcontracts with the U.S. Government are provisional payments, which are subject to potential adjustments upon audit by the Defense Contract Audit Agency (DCAA). Audits through March 31, 2006 have been completed. In the opinion of management, adjustments resulting from the audits of all subsequent years are not expected to have a material effect on the Company's financial position, results of operations, or cash flows.

Litigation

S.C. Diamond Litigation, Virginia Beach Circuit Court On April 2, 2009, SC Diamond Associates, L.P. (S.C. Diamond) filed a lawsuit in Virginia Beach Circuit Court against the Company and Allied Technology Group, Inc. (Allied). S.C. Diamond is the owner of a warehouse property in Virginia Beach, Virginia in which the Company subleased a portion of the facility. In March 2008, the warehouse caught fire, allegedly as a result of an exploded high-intensity metal halide bulb, which is alleged to have been manufactured by Philips Electronics N.A. Corporation, d/b/a Philips Lighting Company (Philips). S.C. Diamond has sued Allied, as its tenant, and the Company, as sub-lessee, alleging breach of contract and negligence against Allied, and negligence against the Company. S.C. Diamond seeks to recover approximately \$12 million in damages from Allied and the Company. Travelers Indemnity Company, which insured S.C. Diamond, intervened in the lawsuit on September 15, 2009, making subrogation claims against Stanley and Philips, seeking to recover approximately \$8 million in insurance proceeds previously paid to S.C. Diamond.

The Company disputes all the allegations against it, and have joined Allied and Travelers in a third-party action against

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Philips, alleging that Philips is liable for the warehouse fire. The Company is being defended in this action by its general liability insurer, which has issued a reservation of rights. In management's opinion, the disposition of this litigation is not expected to have a material adverse effect on the Company's financial position, results of operations or liquidity.

Other Litigation Other than as set forth above, neither the Company, nor any of its subsidiaries, are currently subject to any material legal proceedings, nor, to its knowledge, is any material legal proceeding currently threatened against the Company.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion in conjunction with the unaudited and audited consolidated financial statements and the accompanying notes included in this Form 10-Q and in our Annual Report on Form 10-K for the fiscal year ended March 31, 2009, filed by us with the Securities and Exchange Commission on May 21, 2009. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from those discussed in or implied by any of the forward-looking statements as a result of various factors, including but not limited to, those listed in the Risk Factors section of this Report, as well as in our Annual Report on Form 10-K for the fiscal year ended March 31, 2009. We caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made. We are under no duty to update any of the forward-looking statements after the date of this Quarterly Report on Form 10-Q to conform these statements to actual results, except as required by law.

Overview

We provide information technology services and solutions to U.S. defense, intelligence and federal civilian government agencies. We offer our customers solutions and expertise to support their mission-essential needs at any stage of program, product development or business lifecycle through five service areas: systems engineering, enterprise integration, operational logistics, business process outsourcing and advanced engineering and technology. As a systems integrator, we apply these five service areas to enable our customers to achieve interoperability between different business processes and information technology systems.

Contracts funded by federal government agencies account for substantially all of our revenues. As of September 25, 2009, we had approximately 300 active contractual engagements across more than 50 federal government agencies. Our customers include all major agencies of the Department of Defense, the Department of State, the Department of Homeland Security, the Department of Transportation, the Department of the Treasury, NASA, the Department of Justice and the Department of Health and Human Services.

Key Metrics Evaluated By Management

We manage and assess the performance of our business by evaluating a variety of financial and non-financial metrics derived from and in addition to our United States generally accepted accounting principles, or GAAP, results. The most significant of these metrics are discussed below.

Revenue Growth

We closely monitor revenue growth in order to assess the performance of our business. In monitoring this growth, we focus on both internal revenue growth and revenue growth through acquisitions. Our internal revenue growth is driven primarily by two factors. First, internal revenue growth is driven by adding new customers. For example, over the past several years we have added the Department of Homeland Security's Citizenship and Immigration Services, the Department of the Treasury's Office of the Comptroller of the Currency, the National Guard Bureau, the Department of Transportation and agencies in the intelligence community as new customers. Second, internal revenue growth is driven by

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increasing revenues with existing customers by adding new contracts or expanding existing contracts. For example, since the initial award of our contract with the Department of State for the provision of passport processing and support services, the scope of services provided by us, and the revenues generated by those services, have grown significantly.

Our revenue growth strategy also includes the pursuit of strategic acquisitions. We have completed the following six acquisitions since 2000:

Acquired Company	Date of Acquisition
GCI Information Services, Inc.	January 2000
CCI, Incorporated	September 2002
Fuentez Systems Concepts, Inc.	December 2003
Morgan Research Corporation	February 2006
Techrizon, LLC	April 2007
Oberon Associates, Inc.	July 2008

For further information on our acquisition of Oberon Associates, Inc. (Oberon), please see Note 7 to the Condensed Consolidated Financial Statements, included elsewhere in this report.

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We monitor backlog, which provides us with visibility of our future revenues, as a reflection of our competitive success in our target markets and our ability to retain existing contracts and win new contracts. The following table summarizes our backlog as of the dates indicated:

	September 25, 2009	As of (in millions)	September 26, 2008
Backlog:			
Funded	\$	360.0	\$ 354.6
Unfunded		1,626.4	1,729.5
Total Backlog	\$	1,986.4	\$ 2,084.1

Each year, a significant portion of our revenues is derived from our backlog, and a significant portion of our backlog represents work related to the continuation of services and solutions under contracts or projects where we are the incumbent provider.

We define backlog as the amount of revenues we expect to realize (i) over the remaining base contract performance period and (ii) from the exercise by the customer of option periods that we reasonably believe will be exercised, in each case from signed contracts in existence as of the measurement date. We do not include contract ceiling values, which represent the maximum amount of contract awards that could be awarded to all contractors under government-wide acquisition contracts or agency-specific indefinite delivery/indefinite quantity contracts in our backlog calculation.

We also do not include in backlog (i) the expected amount of revenues that would be realized if, and when, we were successful in the re-compete of signed contracts in existence as of the measurement date, or (ii) the expected amount of revenues that would be realized from future unidentified growth on signed contracts and task orders in existence as of the measurement date.

We define funded backlog as the portion of our backlog for which funding currently is appropriated and obligated to us under a signed contract or task order by the purchasing agency, or otherwise authorized for payment to us by a customer upon completion of a specified portion of work, less the amount of revenue we have previously recognized under the contract. Our funded backlog does not include the full potential value of our contracts because Congress often appropriates funds to be used by an agency for a particular program or contract on a yearly or quarterly basis, even though the contract may call for performance over a number of years. As a result, contracts typically are only partially funded at any point during their term, and all or some of the work to be performed under the contracts may remain unfunded unless and until Congress makes subsequent appropriations and the procuring agency allocates funding to the contract.

Contract Mix

We work with the federal government under contracts employing one of three types of price structures: cost-plus-fee, time-and-materials and fixed-price. Cost-plus-fee contracts are typically lower risk arrangements and thus yield lower profit margins than time-and-materials and

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fixed-price arrangements. Because the customer usually specifies the type of contract for a particular contractual engagement, we generally do not influence the choice of contract type. However, where we do have the opportunity to influence the contract type, and where customer requirements are clear, we prefer time-and-materials and fixed-price arrangements rather than cost-plus-fee arrangements because time-and-materials and fixed-price contracts, as compared with cost-plus-fee contracts, generally provides us with a greater opportunity to generate higher margins and provides the customer with a fixed value for services provided.

The following table summarizes our historical contract mix, measured as a percentage of total revenues, for the periods indicated:

	Three Months Ended		Six Months Ended	
	September 25, 2009	September 26, 2008	September 25, 2009	September 26, 2008
Cost-plus-fee	29%	30%	29%	32%
Time-and-materials	50%	55%	50%	51%
Fixed-price	21%	15%	21%	17%

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Headcount and Labor Utilization

We generate revenues primarily from services provided by our employees and subcontractors, with services provided by our employees generally yielding higher profits than services provided by our subcontractors. Our ability to hire and deploy additional qualified employees is a key driver of our ability to generate additional revenues, and our successful deployment of existing employees on direct-billable jobs is a key driver of our profitability.

Indirect Costs

Indirect costs constitute a substantial portion of the costs associated with our performance of contracts. We carefully monitor the amount by which our actual indirect costs under our contracts vary from those expected to be incurred, which we refer to as indirect expense variance. Increased indirect rates can adversely affect our ability to achieve attractive contract pricing, our profitability, and our competitive position, by resulting in unexpected increased costs to our customers.

Days Sales Outstanding

Days sales outstanding, or DSO, is a measure of how efficiently we manage the billing and collection of our accounts receivable, our most significant working capital requirement. For the three months ended September 25, 2009, we reported DSO of 79 days, a decrease from 84 days for the three months ended June 26, 2009. The decrease in DSO was primarily the result of the timing of receipts from customers and a lower average accounts receivable balance during the quarter.

Unbilled Receivables

Unbilled receivables are comprised of work-in-process that will be billed in accordance with contract terms and delivery schedules, as well as amounts billable upon final execution of contracts, contract completion, milestones or completion of rate negotiations. Because the billing of unbilled receivables is contingent on those events, changes in the relative amount of unbilled receivables have an impact on our working capital and liquidity.

Payments to us for performance on certain of our federal government contracts are subject to audit by the DCAA and are also subject to government funding. We provide a reserve against our receivables for estimated losses that may result from rate negotiations, audit adjustments and/or government funding availability. To the extent that actual adjustments due to rate negotiations, audit adjustments or government funding availability differ from our estimates, our revenue may be impacted. Because substantially all of our receivables come from contracts funded by the federal government, we believe that the likelihood of a material loss on an uncollectible account from this activity is low.

Critical Accounting Policies

The discussion and analysis of our financial condition and results of operations is based on our condensed consolidated financial statements, which have been prepared in accordance with GAAP. The preparation of our condensed consolidated financial statements requires management to make estimates and assumptions that affect reported amounts, and actual results may differ from the estimates. Our significant accounting policies are described in Note 2 to our unaudited condensed consolidated financial statements included elsewhere in this report.

We consider the following accounting policies to be critical to the understanding of our financial condition and results of operations because these policies require the most difficult, subjective or complex judgments on the part of our management in their application, often as a result of the need to make estimates about the effect of matters that are inherently uncertain, and are the most important to our financial condition and operating results.

Revenue Recognition

We recognize revenue under our contracts when a contract has been executed, the contract price is fixed and determinable, delivery of services or products has occurred and collectibility is considered probable and can be reasonably estimated. Revenue is earned under cost-plus-fee, fixed-price and time-and-materials contracts. We use a standard management process to determine whether all required criteria for revenue recognition have been met, which includes regular reviews of our contract performance. This review covers, among other matters, progress against a schedule, outstanding action items, effort and staffing, quality, risks and issues, subcontract management, costs incurred, commitments and customer satisfaction. During this review, we determine whether the overall progress on a contract is consistent with the effort expended.

Contract revenue recognition inherently involves the use of estimates. Examples of estimates include the contemplated level of

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effort to accomplish the tasks under the contract, the cost of the effort and an ongoing assessment of our progress toward completing the contract. From time to time, as part of our standard management process, facts develop that require us to revise our estimated total costs and revenues. To the extent that a revised estimate affects contract profit or revenue previously recognized, we record the cumulative effect of the revision in the period in which the facts requiring the revision become known. The full amount of an anticipated loss on any type of contract is recognized in the period in which it becomes probable and can be reasonably estimated.

Under cost-plus-fee contracts, revenues are recognized as costs are incurred and include an estimate of applicable fees earned. For level of effort or term cost-plus-fee contracts, fixed fees are earned in proportion to the percentage of required effort delivered. We consider fixed fees under cost-plus-fee contracts to be earned in proportion to the allowable costs actually incurred in performance of the contract for level of effort contracts. For completion type cost-plus-fee contracts, fixed fees are earned in proportion to the percentage of work completed. For time-and-materials contracts, revenues are computed by multiplying the number of direct labor-hours expended in performance of the contract by the contractual billing rates and adding other billable direct and indirect costs. For fixed-price contracts, revenues are recognized as services are performed, using the percentage-of-completion method, applying the cost-to-cost or units of delivery method.

For cost-plus-award fee type contracts, we recognize the expected fee to be awarded by the customer at the time such fee can be reasonably estimated, based on factors such as prior award experience and communication with the customer regarding performance, including any interim performance evaluations rendered by the customer. For cost-plus-incentive fee type contracts, the method of calculating the incentive fee is specified in the contract and it is typically based on measuring actual costs to perform the contract against a target cost to perform the contract. We prepare periodic estimates to complete the contract and adjust the incentive fee as required based on the contract incentive fee formula.

Our contracts with agencies of the government are subject to periodic funding by the respective contracting agency. Funding for a contract may be provided in full at inception of the contract or ratably throughout the contract as the services are provided. From time to time, we may proceed with work based on customer direction prior to the completion and signing of formal contract documents. Such situations require completion of a formal internal review process and management approval prior to commencement of work. Additionally, revenue associated with such work is recognized without profit and only when it can be reliably estimated and realization is probable. We base our estimates on notices to proceed from our customers, previous experience with customers, communications with customers regarding funding status, and our knowledge of available funding for the contract or program. Pre-contract costs related to unsuccessful contract bids are expensed in the period in which we are notified that the contract will not be issued.

Disputes occasionally arise in the normal course of our business due to events such as delays, changes in contract specifications, and questions of cost allowability or collectibility. Such matters, whether claims or unapproved change orders in the process of negotiation, are recorded at the lesser of their estimated net realizable value or actual costs incurred, and only when the realization is probable and can be reliably estimated. Claims against us are recognized where a loss is considered probable and can be reasonably estimated in amount.

The allowability of certain costs under government contracts is subject to audit by the government. Certain indirect costs are charged to contracts using provisional or estimated indirect rates, which are subject to later revision based on government audits of those costs. Management is of the opinion that costs subsequently disallowed, if any, would not be significant.

Contract Cost Accounting

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As a contractor providing services primarily to the federal government, we must categorize our costs as either direct or indirect and allowable or unallowable. Direct costs are those costs that are identified with specific contracts. These costs include labor, travel, subcontractor and consultant services, third party materials we purchase under a contract and other non-labor costs incurred in support of a contract. Indirect costs are those costs not identified with specific contracts. Rather, indirect costs are allocated to contracts in accordance with federal government rules and regulations. These costs typically include certain of our selling, general and administrative expenses, fringe benefit expenses, overhead expenses and depreciation and amortization costs. Direct and indirect costs that are not allowable under the Federal Acquisition Regulation or specific contract provisions cannot be considered for reimbursement under our federal government contracts. We must specifically identify these costs to ensure we comply with these requirements. Our unallowable costs include a portion of our executive compensation, certain employee morale activities, certain types of legal and consulting costs, interest expense and the amortization of identified intangible assets, among others.

Goodwill and Intangible Assets

Goodwill represents the excess of cost over the fair value of net tangible and identifiable intangible assets of acquired companies. We do not amortize goodwill. We test goodwill for impairment at least on an annual basis. Testing for impairment is a

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two-step process. The first step is a test for potential impairment, while the second step measures the amount of impairment, if any. We are required to perform an impairment test at least on an annual basis at any time during the fiscal year, provided that the test is performed at the same time every year. An impairment loss would be recognized when the asset's fair value is below its carrying value. We have elected the last day of our third fiscal quarter as our testing date. Based on the testing performed as of December 26, 2008, we determined that no impairments existed. Customer relationships are amortized on a straight-line basis over periods ranging from five to seven years. Non-competition agreements are amortized on a straight-line basis over three years. Backlog and contracts are amortized on a straight-line basis over periods ranging from two to five years.

Results of Operations

Our historical financial statements reflect the operating results of Oberon from July 15, 2008, the date of acquisition. The following unaudited tables set forth the results of operations expressed in thousands of dollars and as a percentage of revenues, for the periods below:

Consolidated Statements of Income Data	Three Months Ended		Six Months Ended	
	September 25, 2009	September 26, 2008	September 25, 2009	September 26, 2008
Revenues	\$ 217,089	\$ 191,078	\$ 425,835	\$ 363,645
Operating costs and expenses:				
Cost of revenues	180,518	159,925	353,607	305,684
Selling, general and administrative	13,401	12,224	27,492	22,883
Depreciation and amortization	2,852	2,586	5,682	4,428
Total operating costs and expenses	196,771	174,735	386,781	332,995
Operating income	20,318	16,343	39,054	30,650
Other income (expense):				
Other income		1	3	3
Interest income	21	71	59	196
Interest expense	(897)	(1,830)	(2,045)	(2,367)
Total other expenses	(876)	(1,758)	(1,983)	(2,168)
Income before taxes	19,442	14,585	37,071	28,482
Provision for income taxes	(7,689)	(5,857)	(14,654)	(11,437)
Net income	\$ 11,753	\$ 8,728	\$ 22,417	\$ 17,045

As a Percentage of Revenues	Three Months Ended		Six Months Ended	
	September 25, 2009	September 26, 2008	September 25, 2009	September 26, 2008
Revenues	100.0%	100.0%	100.0%	100.0%
Operating costs and expenses:				
Cost of revenues	83.2	83.7	83.0	84.1
Selling, general and administrative	6.2	6.4	6.5	6.3
Depreciation and amortization	1.3	1.4	1.3	1.2
Total operating costs and expenses	90.6	91.4	90.8	91.6
Operating income	9.4	8.6	9.2	8.4
Other income (expense):				
Other income				
Interest income				0.1
Interest expense net	(0.4)	(0.9)	(0.5)	(0.7)
Total other expenses	(0.4)	(0.9)	(0.5)	(0.6)
Income before taxes	9.0	7.7	8.7	7.8

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Provision for income taxes	(3.6)	(3.1)	(3.4)	(3.1)
Net income	5.4%	4.6%	5.3%	4.7%

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We generate revenues primarily from services provided by our employees and subcontractors, with services provided by our employees generally yielding higher profits than services provided by our subcontractors. To a lesser degree, we earn revenues through reimbursable travel and other reimbursable direct and indirect costs to support the contractual effort and third-party hardware and software that we purchase and integrate for customers as part of the solutions we provide.

Our most significant expense is cost of revenues, which includes the costs of direct labor, subcontractors, materials, equipment, non-reimbursable travel and an allocation of indirect costs (other than selling, general and administrative expenses and depreciation). Indirect costs consist primarily of fringe benefits, human resources, recruiting, training, other overhead and certain other non-direct costs that are necessary to support direct labor. The number and types of personnel, their salaries and other costs, can have a significant impact on our cost of revenues.

Our selling, general and administrative expenses include costs not directly associated with performing work for our customers. These costs include wages plus associated fringe benefits, stock-based compensation charges, rent, travel, insurance and professional fees. Among the functions covered by these expenses are sales, business development, contract administration, legal, finance, accounting, human resources, information technology and general management. Most of these costs are allowable costs under the cost accounting standards for contracting with the federal government and are recoverable under cost-plus-fee contracts.

Our depreciation and amortization expenses include the amortization of purchased intangibles in connection with acquisitions, the amortization of leasehold improvements and the depreciation of property and equipment purchased in the ordinary course of business.

Certain revenues and payments we receive are based on provisional billings and payments that are subject to adjustment after audit. Federal government agencies have the right to challenge our cost estimates and allocation methodologies with respect to government contracts. In addition, contracts with these agencies are subject to audit and possible adjustment to give effect to unallowable costs under cost-plus-fee contracts or to other regulatory requirements affecting both cost-plus-fee and fixed-price contracts.

Comparison of Results of Operations for the Three Months Ended September 25, 2009 and September 26, 2008

Revenues. Our consolidated revenues increased \$26.0 million, or 13.6%, from \$191.1 million for the three months ended September 26, 2008, to \$217.1 million for the three months ended September 25, 2009. The increase was primarily due to \$10.4 million of increased revenues attributable to military intelligence training and operations support for the U.S. Army, \$5.4 million of increased revenues attributable to procurement, production and engineering services under various SPAWAR contracts, \$5.2 million of increased revenues attributable to information technology and systems support for the U.S. Marine Corps, \$2.7 million of increased revenues attributable to engineering, technical, and program management services to provide full life cycle engineering services for the Naval Sea Logistics Center, and \$2.2 million of increased revenues attributable to biometric software development, training and support for certain agencies in the Department of Defense, offset by \$4.4 million of decreased revenues due to reduced demand for passport services for the Department of State. The balance of increased revenues was primarily a result of engineering and technical support services for the U.S. Air Force and the Defense Information Systems Agency and information technology life cycle support and logistics management services for the U.S. Army.

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Cost of Revenues. Our cost of revenues increased \$20.6 million, or 12.9%, from \$159.9 million for the three months ended September 26, 2008, to \$180.5 million for the three months ended September 25, 2009. This increase was primarily the result of additional costs attributable to revenues associated with the increased services referred to above. Cost of revenues represented 83.2% of revenues for the three months ended September 25, 2009, as compared to 83.7% of revenues for the three months ended September 26, 2008. This decrease was primarily the result of a greater percentage of more profitable fixed price contracts.

Selling, General and Administrative. Our selling, general and administrative expense increased \$1.2 million, or 9.6%, from \$12.2 million for the three months ended September 26, 2008, to \$13.4 million for the three months ended September 25, 2009. This increase was primarily due to an increase in costs to support our growing revenue base and an increase in business development costs. Selling, general and administrative expense represented 6.2% of revenues for the three months ended September 25, 2009, as compared to 6.4% of revenues for the three months ended September 26, 2008. This decrease was primarily a result of efficiencies realized in our corporate infrastructure.

Depreciation and Amortization. Our depreciation and amortization expense increased \$0.3 million, or 10.3%, from \$2.6 million for the three months ended September 26, 2008, to \$2.9 million for the three months ended September 25, 2009. The increase in depreciation and amortization was primarily due to depreciation expense associated with additional property and equipment to support our growth.

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Interest Expense. Our interest expense decreased \$0.9 million, or 51.0%, from \$1.8 million for the three months ended September 26, 2008, to \$0.9 million for the three months ended September 25, 2009. The decrease in interest expense was primarily due to a lower overall borrowing rate, coupled with a lower overall outstanding debt balance.

Provision for Income Taxes. Our effective tax rate decreased 0.7% from 40.2% for the three months ended September 26, 2008, to 39.5% for the three months ended September 25, 2009. The decrease was primarily attributable to a lower consolidated effective state income tax rate.

Net Income. Our net income increased \$3.1 million, or 34.7%, from \$8.7 million for the three months ended September 26, 2008, to \$11.8 million for the three months ended September 25, 2009. The primary reasons for the increase in net income were higher revenues and increased operating income as well as improved margins primarily due to a larger percentage of more profitable fixed-price contracts.

Comparison of Results of Operations for the Six Months Ended September 25, 2009 and September 26, 2008

Revenues. Our consolidated revenues increased \$62.2 million, or 17.1%, from \$363.6 million for the six months ended September 26, 2008, to \$425.8 million for the six months ended September 25, 2009. The increase was primarily due to \$25.8 million of increased revenues attributable to military intelligence training and operations support for the U.S. Army, \$11.6 million of increased revenues attributable to biometric software development, training and support for certain agencies in the Department of Defense, \$11.4 million of increased revenues attributable to engineering and technical support services, primarily for the U.S. Air Force and the Defense Information Systems Agency, \$8.6 million of increased revenues attributable to information technology and systems support for the U.S. Marine Corps, \$7.2 million of increased revenues attributable to procurement, production and engineering services under various SPAWAR programs, and \$4.6 million of increased revenues attributable to engineering, technical, and program management services to provide full life cycle engineering services for the Naval Sea Logistics Center, offset by \$15.9 million of decreased revenues due to reduced demand for passport services for the Department of State. The balance of increased revenues was primarily a result of information technology life cycle support and logistics management services for the U.S. Army. A significant portion of this growth was due to the impact of the contracts obtained as part of the Oberon acquisition.

Cost of Revenues. Our cost of revenues increased \$47.9 million, or 15.7%, from \$305.7 million for the six months ended September 26, 2008, to \$353.6 million for the six months ended September 25, 2009. This increase was primarily the result of additional costs attributable to revenues associated with the increased services referred to above. Cost of revenues represented 83.0% of revenues for the six months ended September 25, 2009, as compared to 84.1% of revenues for the six months ended September 26, 2008. This decrease was primarily the result of a greater percentage of more profitable fixed price contracts.

Selling, General and Administrative. Our selling, general and administrative expense increased \$4.6 million, or 20.1%, from \$22.9 million for the six months ended September 26, 2008, to \$27.5 million for the six months ended September 25, 2009. This increase was primarily due to higher share-based payment expenses, an increase in business development costs and higher selling, general and administrative expenses attributable to the acquisition of Oberon. Selling, general and administrative expense represented 6.5% of revenues for the six months ended September 25, 2009, as compared to 6.3% of revenues for the six months ended September 26, 2008. This increase was primarily a result of higher selling, general and administrative expense as a percentage of revenues associated with supporting contracts and operations that were obtained as part of the Oberon acquisition.

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Depreciation and Amortization. Our depreciation and amortization expense increased \$1.3 million, or 28.3%, from \$4.4 million for the six months ended September 26, 2008, to \$5.7 million for the six months ended September 25, 2009. The increase in depreciation and amortization was primarily due to the amortization of intangible assets associated with the acquisition of Oberon as well as depreciation expense associated with capital expenditures and leasehold improvements.

Interest Income. Our interest income decreased \$0.1 million from \$0.2 million for the six months ended September 26, 2008, to \$0.1 million for the six months ended September 25, 2009. The decrease in interest income was primarily due to a decrease in the number of delayed payments received from customers.

Interest Expense. Our interest expense decreased \$0.4 million, or 13.6%, from \$2.4 million for the six months ended September 26, 2008, to \$2.0 million for the six months ended September 25, 2009. The decrease in interest expense was primarily due to a lower overall borrowing rate, partially offset by borrowings under our Senior Credit Facility relating to the Oberon acquisition.

Provision for Income Taxes. Our effective tax rate decreased 0.7% from 40.2% for the six months ended September 26, 2008, to 39.5% for the six months ended September 25, 2009. The decrease was primarily attributable to a lower consolidated effective state income tax rate.

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Net Income. Our net income increased \$5.4 million, or 31.5%, from \$17 million for the six months ended September 26, 2008, to \$22.4 million for the six months ended September 25, 2009. The primary reasons for the increase in net income were higher revenues and increased operating income as well as improved margins primarily due to a larger percentage of more profitable fixed-price contracts.

Liquidity and Capital Resources

Short-Term Liquidity Requirements. We generally consider our short-term liquidity requirements to consist primarily of funds necessary to finance the costs of operations pending the billing and collection of accounts receivable. We expect to meet our short-term liquidity needs through existing cash balances and cash provided by our operations and, if necessary, from borrowings under our Senior Credit Facility (defined below).

Long-Term Liquidity Requirements. We generally consider our long-term liquidity requirements to consist primarily of funds necessary to pay scheduled debt maturities, non-recurring capital expenditures and the costs associated with acquisitions that we may pursue. Historically, we have satisfied our long-term liquidity requirements through various sources of capital, including cash provided by operations, equity offerings and borrowings under our Senior Credit Facility.

We believe that these sources of capital will continue to be available to us in the future to fund our long-term liquidity requirements. However, our ability to incur additional debt is dependent upon a number of factors, including our degree of leverage, the value of our unencumbered assets, borrowing restrictions imposed by existing lenders and general market conditions. In addition, our ability to raise funds through the issuance of equity securities is dependent upon, among other things, general market conditions and market perceptions about us. We will continue to analyze which source of capital is most advantageous to us at any particular point in time, but the equity markets may not be consistently available on terms that are attractive, or at all.

We expect we will require additional borrowings, including borrowings under our Senior Credit Facility, to satisfy our long-term liquidity requirements. Other sources of liquidity may be sales of common or preferred stock.

Cash Flows

Accounts receivable represents our largest working capital requirement. We bill most of our customers monthly after services are rendered. Our operating cash flow is primarily affected by the overall profitability of our contracts, our ability to invoice and collect from our customers in a timely manner, and our ability to manage our vendor payments.

	Six Months Ended	
	September 25, 2009	September 26, 2008
	(in millions)	
Net cash provided by operating activities	\$ 28.6	\$ 33.2

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Net cash used in investing activities	\$	(2.6)	\$	(172.9)
Net cash (used in) provided by financing activities	\$	(19.5)	\$	152.9

Net cash provided by operating activities of \$28.6 million for the six months ended September 25, 2009 primarily reflected the increased earnings as a result of the improved profitability of our contracts and decrease in accounts receivable due to the timing of collections, partially offset by an increase in prepaid income taxes. Net cash provided by operating activities of \$33.2 million for the six months ended September 26, 2008 primarily reflected our net income plus depreciation and amortization expenses, \$2.8 million of share-based payment expenses for that period, \$2.2 million of income tax benefits from stock compensation and a significant decrease in accounts receivable due to the receipt of delayed payments from several key customers.

Net cash used in investing activities of \$2.6 million for the six months ended September 25, 2009 consisted primarily of purchases of office equipment and leasehold improvements to support our continued growth in operations. Net cash used in investing activities of \$172.9 million for the six months ended September 26, 2008 consisted primarily of \$167.8 million for the purchase of Oberon and the purchase of property, equipment and leasehold improvements associated with new facilities.

Net cash used in financing activities of \$19.5 million for the six months ended September 25, 2009 consisted primarily of \$21.3 million in payments on our revolving portion of our Senior Credit Facility, partially offset by \$1.6 million in proceeds from the exercise of stock options. Net cash provided by financing activities for the six months ended September 26, 2008 consisted primarily of borrowings under our revolving portion of our Senior Credit Facility to support the acquisition of Oberon.

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As of September 25, 2009, we had \$8.3 million in available cash.

Credit Facility and Borrowing Capacity

We are party to a credit agreement (Senior Credit Facility or Amended Credit Agreement) with a group of lenders for which SunTrust Robinson Humphrey, Inc. acted as sole book manager and lead arranger, SunTrust Bank acted as administrative agent and M&T Bank and BB&T Bank acted as co-documentation agents.

At September 25, 2009, the lenders aggregate commitment under the Senior Credit Facility was \$276.9 million, which consisted of a \$241.6 million revolving line of credit (Revolver) and a \$35.3 million term loan (Term Loan), and we had outstanding indebtedness of \$35.3 million on the Term Loan and \$113.7 million on the Revolver, with a weighted-average interest rate of approximately 1.70% and 3.75% for the six months ended September 25, 2009 and September 26, 2008, respectively. At September 25, 2009, our borrowing availability under the Senior Credit Facility was \$127.9 million, including outstanding letters of credit. Under the terms of the Amended Credit Agreement, we may request an increase in the size of the Revolver by an aggregate amount not greater than \$33.4 million. If any lender elects not to increase its commitment, we may designate another bank or other financial institution to become a party to the Amended Credit Agreement.

The Amended Credit Agreement also contains a number of affirmative and restrictive covenants, including limitations on mergers, consolidations and dissolutions; sales of assets; investments and acquisitions; indebtedness and liens; repurchases of shares of capital stock and options to purchase shares of capital stock; transactions with affiliates; sale and leaseback transactions; and restricted payments.

In addition, the Amended Credit Agreement requires us to meet the following financial covenants:

- a fixed charge coverage ratio as of the end of any fiscal quarter of not less than 1.35 to 1.00, based upon the ratio of (i) consolidated EBITDA (as defined in the Amended Credit Agreement) less the actual amount paid by us and our subsidiaries in cash on account of capital expenditures and taxes to (ii) consolidated interest expense for such period, scheduled principal payments required to be made on consolidated total debt during such period and certain restricted payments paid during such period, in each case measured for the four consecutive fiscal quarters ending on or immediately prior to such date; and
- a maximum leverage ratio not greater than 3.75 to 1.00, based upon the ratio of (i) consolidated total debt to (ii) consolidated EBITDA (as defined in the Amended Credit Agreement).

At September 25, 2009, we were in compliance with all covenants under our Senior Credit Facility. The obligations under the Senior Credit Facility are unconditionally guaranteed by each of our existing and subsequently acquired or organized subsidiaries and are secured on a first-priority basis by security interests (subject to permitted liens) in substantially all assets owned by us and each of our subsidiaries, including the shares of capital stock of our subsidiaries, subject to certain exceptions.

Capital Expenditures

Our capital expenditures were \$2.6 million and \$5.1 million for the six months ended September 25, 2009 and September 26, 2008, respectively. Substantially all of these expenditures consisted of leasehold improvements and purchases of office equipment.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements as defined in Item 303(a)(4)(ii) of SEC Regulation S-K as of September 25, 2009.

Recent Accounting Pronouncements

In June 2009, the FASB issued Statement of Financial Accounting Standards No. 168, *The FASB Accounting Standards Codification* (Codification) and the *Hierarchy of Generally Accepted Accounting Principles* (GAAP), a replacement of FASB Statement No. 162 (SFAS 168). SFAS 168 establishes the Codification as the single source of authoritative GAAP in the United States, other than rules and interpretive releases issued by the SEC. The Codification is a reorganization of current GAAP into a topical format that eliminates the current GAAP hierarchy and establishes instead two levels of guidance authoritative and

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nonauthoritative. All non-grandfathered, non-SEC accounting literature that is not included in the Codification will become nonauthoritative. The FASB's primary goal in developing the Codification is to simplify user access to all authoritative GAAP by providing all the authoritative literature related to a particular accounting topic in one place. The Codification was effective for interim and annual periods ending after September 15, 2009. Following SFAS 168, the Board will not issue new standards in the form of Statements, FASB Staff Positions, or Emerging Issue Task Force Abstracts; instead, it will issue Accounting Standards Updates. The FASB will not consider Accounting Standards Updates as authoritative in their own right; these updates will serve only to update the Codification, provide background information about the guidance, and provide the bases for conclusions on the change(s) in the Codification. In the description of Accounting Standards Updates that follows, references in *italics* relate to Codification Topics and Subtopics, and their descriptive titles, as appropriate.

Accounting Standards Updates In June 2009, an update was made to *Consolidation Consolidation of Variable Interest Entities*. Among other things, the update replaces the calculation for determining which entities, if any, have a controlling financial interest in a variable interest entity (VIE) from a quantitative based risks and rewards calculation, to a qualitative approach that focuses on identifying which entities have the power to direct the activities that most significantly impact the VIE's economic performance and the obligation to absorb losses of the VIE or the right to receive benefits from the VIE. The update also requires ongoing assessments as to whether an entity is the primary beneficiary of a VIE (previously, reconsideration was only required upon the occurrence of specific events), modifies the presentation of consolidated VIE assets and liabilities, and requires additional disclosures about a company's involvement in VIEs. This update will be effective for fiscal years beginning after November 15, 2009. We do not currently believe that the adoption of this update will have any effect on our consolidated financial position and results of operations.

In September 2009, an update was made to *Fair Value Measurements and Disclosures Investments in Certain Entities that Calculate Net Asset Value per Share (or Its Equivalent)*. This update permits entities to measure the fair value of certain investments, including those with fair values that are not readily determinable, on the basis of the net asset value per share of the investment (or its equivalent) if such net asset value is calculated in a manner consistent with the measurement principles in *Financial Services-Investment Companies* as of the reporting entity's measurement date (measurement of all or substantially all of the underlying investments of the investee in accordance with the *Fair Value Measurements and Disclosures* guidance). The update also requires enhanced disclosures about the nature and risks of investments within its scope that are measured at fair value on a recurring or nonrecurring basis. This update will be effective for interim and annual periods ending after December 15, 2009. We are currently evaluating the effect that adoption of this update will have, if any, on our consolidated financial position and results of operations.

In October 2009, an update was made to *Revenue Recognition Multiple Deliverable Revenue Arrangements*. This update removes the objective-and-reliable-evidence-of-fair-value criterion from the separation criteria used to determine whether an arrangement involving multiple deliverables contains more than one unit of accounting, replaces references to fair value with selling price to distinguish from the fair value measurements required under the *Fair Value Measurements and Disclosures* guidance, provides a hierarchy that entities must use to estimate the selling price, eliminates the use of the residual method for allocation, and expands the ongoing disclosure requirements. This update is effective for fiscal years beginning on or after June 15, 2010, and can be applied prospectively or retrospectively. We are currently evaluating the effect that adoption of this update will have, if any, on our consolidated financial position and results of operations.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our principal exposure to market risk relates to changes in interest rates. From time to time, we enter into interest rate swap agreements to limit exposure to interest rate movements within the parameters of our interest rate hedging policy. As of September 25, 2009, all of the outstanding debt under our Senior Credit Facility, with the exception of the portion covered by an interest rate swap, was subject to interest rate risk. In October 2006, we entered into an interest rate swap agreement covering fifty percent of our term indebtedness under which the swap and term debt maturities match. Even after giving effect to this agreement, we remain exposed to risks due to fluctuations in the market value of this agreement and changes in interest rates with respect to the portion of our Senior Credit Facility that is not covered by this swap agreement. A hypothetical increase in the interest rate of 100 basis points would have increased our interest expense for the six months ended September 25, 2009 on that portion of our outstanding debt not covered by the interest rate swap by \$0.7 million.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

As of September 25, 2009, under the supervision and with the participation of our management, including our chief executive officer and our chief financial officer, we have evaluated the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-15 of the Securities Exchange Act of 1934, as amended, or Exchange Act. Based on this evaluation, our chief executive officer and our chief financial officer have concluded that our disclosure controls and procedures are effective in providing reasonable assurance that the information required to be disclosed in this report has been recorded, processed, summarized and reported as of the end of the period covered by this report. In evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Changes in Internal Control over Financial Reporting

There has not been any change in our internal control over financial reporting (as defined in Rule 13a-15(f) of the Exchange Act) identified in connection with the evaluation required by Rule 13a-15(d) under the Exchange Act during the quarter ended September 25, 2009 that has materially affected, or is reasonably likely to materially affect, those controls.

Limitations on the Effectiveness of Controls

Our management, including our chief executive officer and chief financial officer, does not expect that our disclosure controls and procedures and internal controls over financial reporting will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met, and our management has concluded that our disclosure controls and procedures and internal controls over financial reporting were effective at a reasonable assurance level as of September 25, 2009. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls

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must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, with the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people or by management override of the controls.

The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, a control may become inadequate because of changes in conditions or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and may not be detected.

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PART II: OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

S.C. Diamond Litigation Virginia Beach Circuit Court

On April 2, 2009, SC Diamond Associates, L.P. filed a lawsuit in Virginia Beach Circuit Court against us and Allied Technology Group, Inc., or Allied. S.C. Diamond is the owner of a warehouse property in Virginia Beach, Virginia in which we subleased a portion of the facility. In March 2008, the warehouse caught fire, allegedly as a result of an exploded high-intensity metal halide bulb, which is alleged to have been manufactured by Philips Electronics N.A. Corporation, d/b/a Philips Lighting Company, or Philips. S.C. Diamond has sued Allied, as its tenant, and us, as sub-lessee, alleging breach of contract and negligence against Allied, and negligence against us. S.C. Diamond seeks to recover approximately \$12 million in damages from Allied and us. Travelers Indemnity Company, which insured S.C. Diamond, intervened in the lawsuit on September 15, 2009, making subrogation claims against us and Philips, seeking to recover approximately \$8 million in insurance proceeds previously paid to S.C. Diamond.

We dispute all the allegations against us, and have joined Allied and Travelers in a third-party action against Philips, alleging that Philips is liable for the warehouse fire. We are being defended in this action by our general liability insurer, which has issued a reservation of rights. In management's opinion, the disposition of this litigation is not expected to have a material adverse effect on the Company's financial position, results of operations or liquidity.

Other Litigation

Other than as set forth above, neither we, nor any of our subsidiaries, are currently subject to any material legal proceedings, nor, to our knowledge, is any material legal proceeding currently threatened against us.

ITEM 1A. RISK FACTORS

In addition to the other information set forth in this report, you should carefully consider the risks discussed in Part I, Item 1A. Risk Factors in our Form 10-K for the fiscal year ended March 31, 2009. These risks and uncertainties have the potential to affect materially our business, financial condition, results of operation, cash flows and future prospects.

We do not believe that there have been any material changes to the risk factors previously disclosed in our Form 10-K for the fiscal year ended March 31, 2009.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

Table of Contents**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

The Annual Meeting of the Company's Stockholders was held on August 7, 2009. The stockholders voted and approved the following matters:

The election of eight directors to hold office until the 2010 Annual Meeting of Stockholders:

Nominee	Shares Voted For	Votes Withheld
Mr. Philip O. Nolan	22,643,762	523,565
Mr. George H. Wilson	22,539,393	627,934
Mr. William E. Karlson	22,081,397	1,085,930
Mr. James C. Hughes	22,919,741	247,586
Lt. General Richard L. Kelly, USMC (Ret.)	22,937,483	229,844
Mr. Charles S. Ream	22,911,372	255,955
Mr. John P. Riceman	22,945,820	221,507
General Jimmy D. Ross, USA (Ret.)	22,919,115	248,212

The approval of the Amended and Restated 2006 Omnibus Incentive Compensation Plan:

Voted For	Number of Shares Voted Against	Abstained	Broker Non-Votes
13,798,615	7,975,493	32,706	1,360,513

The ratification of the appointment of Deloitte & Touche LLP as independent registered public accounting firm for our fiscal year ending March 31, 2010:

Voted For	Number of Shares Voted Against	Abstained	Broker Non-Votes
22,842,915	309,619	14,793	0

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

See the exhibit index.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned.

STANLEY, INC.

/s/ PHILIP O. NOLAN

Philip O. Nolan
Chairman, President and Chief Executive Officer
(Principal Executive Officer)
October 29, 2009

/s/ BRIAN J. CLARK

Brian J. Clark
Executive Vice President, Chief Financial Officer and Treasurer
(Principal Financial and Accounting Officer)
October 29, 2009

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EXHIBIT INDEX

Exhibit No.	Description
3.1	Amended and Restated Certificate of Incorporation of Stanley, Inc. (incorporated by reference to Exhibit 3.1 to the Company's Form 10-K for the fiscal year ended March 31, 2008)
3.2	Amended and Restated Bylaws of Stanley, Inc. (incorporated by reference to Exhibit 3.2 to the Company's Form 10-K for the fiscal year ended March 31, 2008)
10.1	Stanley, Inc. Amended and Restated 2006 Omnibus Incentive Compensation Plan (incorporated by reference to Exhibit 10.1 to the Company's 8-K, filed on August 7, 2009)
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of The Sarbanes-Oxley Act of 2002.*

* Filed herewith

Denotes management contract or compensation plan or arrangement