

ATSC Q3 2008 Earnings Call Script

OPENING OF CALL/OPERATOR:

OPERATOR: Welcome to the ATS Corporation Third Quarter 2008 Conference Call. During the presentation, all participants will be in a listen-only mode. Afterwards, you will be invited to participate in a question and answer session.

Now I would like to turn the program over to Joann O'Connell, Vice President of Investor Relations.

MODERATOR (J. O'Connell): Thank you. Good afternoon and thank you for joining us to review our third quarter 2008 results. With us this afternoon from ATS Corporation are Ed Bersoff, Chairman, President and Chief Executive Officer, Pamela Little, Executive Vice President and Chief Financial Officer, and George Troendle, Executive Vice President and Chief Operating Officer.

Before I review the structure of this call, I would like to read the safe harbor statement.

This conference call could contain forward looking statements about ATS Corporation within the meaning of the Private Securities Litigation Reform Act of 1995. Forward looking statements are statements that are not historical fact. Such forward looking statements are based upon the current belief and expectations of ATS' management and are subject to risks and uncertainties, which could cause actual results to differ from the forward looking statements. Such risks are more fully discussed in ATS' filings with the Securities and Exchange Commission. The information set forth herein should be considered in light of such risks. ATS Corporation does not assume any obligation to update the information contained in this conference call.

At this time, I would like to outline the agenda for today's call:

- First, Ed will offer opening remarks.
- Next, Pamela will review ATS Corporation's third quarter financial results.
- Next, George will briefly highlight several recent contract wins.
- Finally, Ed will review operating results and offer concluding remarks.
- At the completion of Ed's remarks, the Company will open the call to take your questions.

At this time, I would like to turn the call over to Dr. Edward Bersoff, Chairman, President and Chief Executive Officer of ATS Corporation.

Ed?

OPENING REMARKS:

E. BERSOFF: Good afternoon and thank you all for joining us today to review ATS Corporation's third quarter 2008 financial and operational performance.

Before I discuss those results, I would like to first take the opportunity to welcome George Troendle who will be participating with us on the call today. As we announced last quarter, George joined us in August of this year as Executive Vice President and Chief Operating Officer. George comes to us with extensive experience as the founder, Chief Executive Officer and Director of Resource Consultants, a government services company he grew to over \$300 million before it was acquired by Serco Group in 2005. We're very excited to have George on board and we'll hear from him later regarding some of our recent contract wins.

Now we would like to turn to our third quarter results. Similar to last quarter, this was a quarter of mixed results for us. We experienced an increase in bookings this quarter compared to earlier quarters and for the first time this year, are pleased to report an increase in backlog and a book to bill ratio greater than one. We also continued to meet our EBITDA margin targets and perform well on all our existing contracts. We however, continue to experience revenue weakness, mostly in our commercial business unit. The revenue weakness was as we expected and in line with our guidance for the year. As a result, we've been able to manage our costs accordingly to achieve our target margins. Finally, as we discussed in our earnings release for the quarter, we evaluated the fair market value of our goodwill and intangible assets and determined that we should incur a sizeable non-cash impairment charge. While this has no cash impact, it has created a significant book loss for the quarter which Pamela will discuss in greater detail.

I will further talk about our operational accomplishments and challenges for the quarter and outline our continued initiatives for 2008, after Pamela provides the financial details of the third quarter and George comments on some of our recent contract wins.

Pamela?

FINANCIAL RESULTS:

P. LITTLE: We will begin with our GAAP results, followed by our Earnings Before Interest, Taxes, Depreciation, Amortization and then explain the difference.

For the quarter ended September 30, 2008, we recorded \$32 million in revenue. Revenue for the quarter increased by approximately 25% over the third quarter of 2007 revenue of \$25.6 million. Acquisitions in 2007 strongly influenced the third quarter revenue growth. Revenue from commercial contracts grew slightly, by 3% and revenue from government contracts increased by 24% over the third quarter of 2007.

As Ed mentioned before, we incurred a \$56.8 million non-cash goodwill and intangible asset impairment charge this quarter which had a significant impact on our earnings. The impairment resulted from an updated outlook for the businesses acquired in 2007, which led to an adjustment of the estimated fair market value of the operating subsidiary.

Including the impact of the impairment charge, the operating loss and the net loss for the quarter was \$55.8 million and \$51 million, respectively, or a loss per share of \$2.28 compared to operating income of \$711,000 and net income of \$353,000 for the third quarter of 2007.

Excluding the impact of the impairment charge, we did experience a year over year increase in operating margin in the third quarter. The increase was driven by several factors, including the non recurrence of the extraordinary charges we identified in 2007, a reduction in indirect labor costs, and a full quarter of savings from rent expense generated from our move into a new building.

It is also important to note that we believe that our gross margins will remain in the 29 to 30% range for the rest of this year based on our existing contract base. The decline from earlier quarters this year is due to a shift in our contract mix with some of the recent wins.

Excluding the impact of the impairment charge and the associated tax benefit, the decline in quarterly year over year net income is a result of the interest expense on our line of credit and promissory notes. Our current line of credit was put in place in June of last year. We initially drew on the line for the Potomac Management Group acquisition in early September 2007, but did not draw down significantly on the line until we completed the Number Six Software transaction in November of 2007.

Let me now turn to our internal metrics of performance and highlight how we look at our results. As I said a moment ago, our reported net loss was \$51 million for the quarter. We incurred depreciation and amortization expenses of approximately \$1.5 million of which \$618,000 was related to our acquisition of Advanced Technology Systems, Inc. Subtracting the tax benefit of \$5.8 million and adding the \$56.8 million impairment charge, interest of \$897,000, and \$1.5 million of depreciation and amortization to our net loss results in an actual EBITDA of \$2.5 million and an associated actual EBITDA margin of 7.7%.

As we reported in our third quarter earnings report today, operating expenses included \$890,000 of one-time severance expenses related to the termination of three senior executives this quarter who will not be replaced. Further adjusting EBITDA for the \$890,000 of one-time severance expenses, resulted in an adjusted EBITDA of \$3.4 million and an associated EBITDA margin of 10.5% for the quarter.

Net loss adjusted for the impairment charge and the associated tax benefit and the amortization of Advanced Technology Systems-related intangibles was \$654,000, or \$0.03 per diluted share.

When combined with our first two quarter results, revenue and adjusted EBITDA for the first nine months was \$100.7 million and \$9.6 million, respectively, resulting in an EBITDA margin of 9.6%. Net income for the first nine months adjusted for the impairment charge and associated tax benefit and the amortization of Advanced Technology Systems-related intangibles was \$2.8 million, or \$0.13 per diluted share.

Due to the goodwill and intangible asset impairment charge, we will no longer be tracking amortization separately for each of the businesses acquired in 2007. As a result, this will be the last quarter we will announce the net income and earnings per share adjusted for the Advanced Technology Systems-related intangibles.

In accordance with Reg G, I would like to take a moment to walk you through a reconciliation of the third quarter EBITDA. Our GAAP net loss was reported at \$51 million. To this amount, we subtract a tax benefit of \$5.8 million and add an interest expense of \$897,000. Further adding back the impairment charge of \$56.8 million and our depreciation and amortization expense of \$1.5 million results in a third quarter actual EBITDA of \$2.5 million.

Other measures of performance that we monitor regularly include backlog and days sales outstanding, or DSO. Our contract backlog at September 30 increased to \$208 million, of which \$55 million was funded.

Our DSO at the end of the quarter was at 86 days. While our DSO is still at a higher level than where we expect it should be, we have seen significant cash collections in the third quarter. We believe the DSO will continue to decline over the next few quarters.

As of September 30, 2008, the balance on the revolving credit facility was \$35.8 million and we had approximately \$5.2 million in promissory notes, both related to the acquisitions we made in 2007.

As Ed mentioned earlier, our financial results today are mixed. We are pleased to see the pick up in backlog this quarter. Our revenue continued to show weakness this quarter, although it was in line with our expectations and as a result, we were able to reduce our expenses as necessary to maintain our target EBITDA margins. Furthermore, we were able to generate strong cash flow for the quarter allowing us to pay our line of credit balance down by \$8 million.

Regarding the impairment charge, the weakness in the economy and its particular impact on our commercial business combined with the overall sluggish revenue contributed to the charge. Furthermore, given our heritage as a special purpose acquisition company, our entire operating business was created through acquisitions, including the platform company, resulting in significant goodwill and intangibles recorded on our books that a peer company with an existing operating history would not have on its books. As a result, from the outset, our exposure to a potential impairment charge was increased. We remain optimistic as to the long term performance of the acquisitions and believe the increase in bookings this quarter establish a strong foundation for the company going into 2009 to both return to organic growth and continue strong cash flow generation. This concludes my review of the financials and I would now like to turn the call over to George.

George?

NEW CONTRACT WINS

G. TROENDLE: Thank you, Pamela. As Ed mentioned earlier, I'd like to highlight a couple of noteworthy new contract awards that we obtained in the third quarter.

First, the Department of Housing and Urban Development selected ATSC on a sole source basis for the award of a \$10M, one-year contract for software and systems development support. Under this new contract, ATSC will provide system modifications to support HUD's new responsibilities under the Housing and Economic Recovery Act of 2008, which passed earlier this year to modernize the The Federal Housing Administration and provide new FHA loans to keep eligible families in their homes under the HOPE for Homeowners Program.

Second, we received a \$10M, five-year subcontract from Security Assistance Corporation for mariner professional qualification evaluation support at the United States Coast Guard National Maritime Center. This award sustains ATSC's longstanding role in support of the National Maritime Center, a role that became part of ATSC with the acquisition of Performance Management Group.

Including these two \$10M awards, our total new bookings for the quarter totaled \$53M. The balance consisted mostly of options, extensions, and additional taskings under existing contracts.

In addition to the increased bookings activity experienced in the third quarter, we also saw improved momentum in our business development pipeline. While we have not historically reported details of our pipeline, we plan to do so in future quarters. We are confident that as the quality of our pipeline continues to strengthen, we can sustain the strong quarterly bookings progress demonstrated in the third quarter, thereby positioning the company to achieve its organic growth targets for 2009 and beyond.

Ed?

OPERATING RESULTS

E. BERSOFF: Thank you, George. I would like to take the opportunity to highlight our accomplishments achieved this quarter and our priorities for the rest of the year. These include:

1. Achieving stronger bookings this quarter than previous quarters, resulting in a book to bill ratio greater than one and an increase in our backlog, after a declining trend the past two quarters.
2. Exceeding our targeted EBITDA margin of 9% even with a slight decline in revenue and continued investment in business development.
3. Maintaining strong customer satisfaction as evidenced by our continued strong record of winning our recompetes, such as with the Coast Guard; the emergence of our role as a preferred vendor for Fannie Mae during its transition period; and our expanded role with HUD as it turned to us as one of its long-term trusted partners to modernize its systems in response to the housing recovery efforts.

And

4. Adding a key new board member, Jack Tomarchio, to replace George Troendle, who resigned as a director upon becoming our Chief Operating Officer. Jack is a former Department of Homeland Security executive and we look forward to benefiting from his experience in security and intelligence matters to contribute to our expanding information-sharing capabilities, where we have seen tremendous growth opportunities.

As I stated in earlier calls, we have outlined the following additional priority initiatives for 2008:

1. Supporting the efforts of our business development organization and continuing to increase our bid pipeline and backlog to set the foundation to return to organic growth in 2009 and beyond.
2. Maintaining a 9% EBITDA margin.

3. Continuing to achieve successful Sarbanes-Oxley compliance testing.
4. Although we have previously announced the desire to list on a national exchange this year, our current stock price does not meet the minimum market capitalization requirement. Listing on a national exchange is a top priority and we will pursue that listing as soon as we meet all of the relevant listing requirements.

And

5. Finally we had also hoped to pursue an additional acquisition this year, but appreciate that the current challenging credit environment makes it unlikely that an acquisition would be in our best interests. We will, however continue to use our cash flow generation to pay down our debt and better position ourselves to target and finance acquisitions in 2009.

GUIDANCE AND CONCLUDING REMARKS:

E. BERSOFF: Before we open the call to questions, I'd like to reaffirm our guidance for 2008 of revenue for the year to be \$129 million to \$135 million and EBITDA of \$11.5 million to \$13.0 million.

We continue to remain confident in our ability to achieve our long term growth strategy. Realizing profitable top-line growth remains our number one priority.

This concludes my remarks. At this point, we would like to open the call to questions.

AFTER Q&A:

E. BERSOFF: Thank you for your time and attention. We look forward to speaking with each of you over the coming months and thank you again for your support.