Leidos Holdings, Inc.
Form 10-K
February 19, 2019

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-K

(Mark One)
x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 28, 2018
or
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission File Number: 001-33072
Leidos Holdings, Inc.
(Exact name of registrant as specified in its charter)

Delaware	20-3562868
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
11951 Freedom Drive, Reston, Virginia	20190
(Address of principal executive offices)	(Zip Code)

(571) 526-6000
(Registrant's telephone number, including area code)
Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Leidos Holdings, Inc. Common Stock, Par Value $.0001 Per Share	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:
None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No o
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No x
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o
Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes x No o
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated

filer”, “smaller reporting company”, and "emerging growth company" in Rule 12b-2 of the Exchange Act.
Large accelerated filer x Accelerated filer o Non-accelerated filer o Smaller reporting company o Emerging growth company o
If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. o
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No x
As of June 29, 2018, which was the last business day of the registrant's most recently completed second fiscal quarter, the aggregate market value of Leidos Holdings, Inc. common stock (based upon the closing price of the stock on the New York Stock Exchange) held by non-affiliates of the registrant was $8,841,791,254.
The number of shares issued and outstanding of the registrant’s class of common stock as of February 11, 2019 was 146,160,889 shares ($.0001 par value per share).
DOCUMENTS INCORPORATED BY REFERENCE
Portions of Leidos Holdings, Inc.'s definitive Proxy Statement for the 2019 Annual Meeting of Stockholders ("2019 Proxy Statement") are incorporated by reference in Part III of this Annual Report on Form 10-K.

LEIDOS HOLDINGS, INC.
FORM 10-K
TABLE OF CONTENTS

Table of Contents
PART I

Item 1. Business
Our Company
Leidos Holdings, Inc. ("Leidos"), a Delaware corporation, is a holding company whose direct 100%-owned subsidiary and principal operating company is Leidos, Inc. Leidos was founded in 1969 by physicist Dr. Robert Beyster. Since our founding 50 years ago, we have applied our expertise in science, research and engineering in rapidly evolving technologies and markets to solve complex problems of global concern.
We use the terms "Company," "we," "us" and "our" to refer collectively to Leidos Holdings, Inc. and its consolidated subsidiaries.
Leidos is a FORTUNE 500® science, engineering and information technology company that provides services and solutions in the defense, intelligence, civil and health markets. We bring domain-specific capability and cross-market innovations to customers in each of these markets by leveraging seven core capabilities: enterprise modernization; cyber operations; operations and logistics; mission software systems; integrated systems; sensors and phenomenology; and mission support. Applying our technically advanced solutions to help solve our customers' most difficult problems has enabled us to build strong relationships with key customers. Our domestic customers include the U.S. Department of Defense ("DoD"), the U.S. Intelligence Community, the U.S. Department of Homeland Security ("DHS"), the Federal Aviation Administration ("FAA"), the Department of Veterans Affairs ("VA") and many other U.S. government civilian agencies, as well as state and local government agencies. With a focus on delivering mission-critical solutions, Leidos generated 85% of fiscal 2018 revenues from U.S. government contracts.
Building on our foundation in offering innovative services and solutions to U.S. government customers, Leidos serves international government and broader commercial markets. Our international customers include foreign governments and their agencies, primarily located in Australia and the United Kingdom ("U.K."). By leveraging expertise in multiple disciplines, tailoring our services and solutions to the particular needs of our targeted markets and using advanced analytics, we work to securely deliver services and solutions that not only meet customers' current goals, but also support their future missions.
For additional discussion and analysis related to recent business developments, see "Business Environment and Trends" in "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Part II of this Annual Report on Form 10-K.
Our Business Segments
During fiscal 2017, we completed a business reorganization, which resulted in the identification of new reportable segments. We commenced operating and reporting under the new organization structure effective the beginning of fiscal 2017. As a result of this change, fiscal 2016 segment results and disclosures have been recast to reflect the new reportable segments.
At December 28, 2018, our business is aligned into three reportable segments (Defense Solutions, Civil and Health). Additionally, we separately present the costs associated with corporate functions as Corporate. Our operations and reportable segments are organized around the markets served and the nature of the products and services provided to customers in those markets. We provide a wide array of scientific, engineering and technical services and solutions across these reportable segments. Less than 10% of our revenues and tangible long-lived assets are generated by or owned by entities located outside of the United States.
Defense Solutions
Defense Solutions is focused on rapidly deploying agile, cost-effective solutions to meet the ever-changing missions of our customers in the areas of intelligence surveillance and reconnaissance ("ISR"), enterprise information technology ("IT"), integrated systems, cybersecurity and global services. We provide a diverse portfolio of national security solutions and systems for air, land, sea, space and cyberspace for the U.S. Intelligence Community, the DoD, military services, DHS, government agencies of U.S. allies abroad and other federal, civilian and commercial customers in the national security industry. Our solutions deliver innovative technology, large-scale intelligence systems, command and control platforms, data analytics, logistics and cybersecurity solutions, as well as intelligence

analysis and operations support to critical missions around the world. Defense Solutions represented 48%, 49% and 55% of total revenues for fiscal 2018, 2017 and 2016, respectively.

Our Defense Solutions business offers broad technology, development and integration capabilities and is responsible for leading our efforts in surveillance and reconnaissance, integrated systems solutions and global services for the U.S. Intelligence Community, military commands and other government and commercial customers.

- Surveillance and Reconnaissance – We offer a wide range of technologies in multiple domains that address the nation's most critical threats and deliver solutions to the U.S. Intelligence Community, DoD and military services. A primary focus is on the DoD's technology organizations, which include the Defense Advanced Research Projects Agency, Army Research Lab, Air Force Research Lab and Office of Naval Research. Our market concentration is on airborne and ground ISR, maritime systems, electronic warfare systems, distributed sensor systems, autonomous systems and command and control. We provide multi-spectral, airborne, ground and maritime ISR collection and processing systems, advanced sensor design, command and control solutions and training systems.
- Enterprise IT and Integrated Systems – We offer extensive software development capabilities for intelligence and information systems and deliver mission and enterprise-level solutions to the U.S. and allied Intelligence Community, DoD, military services, DHS and the Australian Department of Defense. Our markets include cybersecurity, data analytics, enterprise IT and operations and logistics. Our cybersecurity solutions detect and manage the most sophisticated cyber threats. We offer innovative data analytics capabilities, and we design, develop, integrate, deploy and support information-centric software and enterprise IT systems for complex, data-driven national security challenges. Our operations and logistics offerings include enterprise platforms that speed the supply chain of highly complex systems.
- Global Services – We provide high-end services to the U.S. Intelligence Community, DoD and federal civilian agencies. Operating around the world daily, we provide intelligence analysis, operational support, security, linguistics and training. In addition, we deliver tailored IT services and solutions to our customers across the globe.

Civil

Our Civil business is focused on seamlessly integrating and protecting physical, digital and data domains. By applying leading science, effective technologies and business acumen, our talented employees help customers maximize their performance and take on the connected world with data-driven insights, improved efficiencies and technological advantages. Civil represented 34%, 33% and 29% of total revenues for fiscal 2018, 2017 and 2016, respectively.

- Aviation Solutions – Leidos is a trusted systems integrator serving Air Navigation Service Providers including the FAA, the Transportation Security Administration ("TSA") and airport operators. Our work in airport modernization helps stakeholders achieve stated objectives, including increased operational efficiency and safety, a technology enhanced passenger experience, non-aeronautical revenue enablement and state-of-the-art situational awareness and security. Leidos air traffic control systems are used in Air Navigation Service Provider facilities that control more than 60 percent of the world's air traffic. We work diligently to support the FAA's NextGen program with government accepted systems including En Route Automation Modernization, Advanced Technology Oceanic Procedures, Time Based Flow Management and Terminal Flight Data Management. For the National Air Traffic Services system in the U.K., we offer the SkyLine Air Traffic Management suite to enhance safety, improve on-time performance and increase fuel efficiency.
- Security Products – Our Vehicle and Cargo Inspection Systems enable the rapid scanning of vehicles and cargo using patented technology that produces a high-quality image using a low radiation dose while using less space and processing higher volumes of cars and trucks than other scanning systems. Our Reveal line of explosive detection systems for checked airline baggage pioneered the "reduced size" segment of this market with small, flexible systems that can be installed at airport check-in counters. We also have a line of radiation detection systems, which are used today at ports, border crossings and industrial facilities around the world – including most ports and border crossings in the United States.

- Enterprise IT Services – We deliver secure, user-centric IT solutions in cloud computing, mobility, application modernization, DevOps, data center and network modernization, asset management, help desk operations and digital workplace enablement. We help our customers achieve their missions and business goals by delivering purpose-built solutions, cybersecurity as a standard, efficient project delivery and end-user satisfaction. Leidos is modernizing enterprise IT for CONUS/OCONUS programs in classified and unclassified environments, including programs with the General Services Administration ("GSA"), the Department of Housing and Urban Development and the Department of Justice.
- Federal Environment and Infrastructure – We are trusted by civilian and defense agencies with substantial environmental and sustainability driven missions. Our pedigree across environmental management, nuclear security, energy efficiency, infrastructure management, mission support and IT modernization provides the applicable expertise needed to transform operations while modernizing aging infrastructure and maintaining environmental stewardship. We support several of the Department of Energy's largest nuclear production, operations and remediation sites. At Hanford, we provide site-wide infrastructure management and operation including oversight of land and logistics, public works, information technology, fleet transportation, environmental sustainability and compliance, first responder services and future project planning. Our environmental engineers and scientists address all aspects of remediation for soil, groundwater, surface water and sediment, including removal, treatment, bioremediation, containment, resource management, land use and institutional controls, air emission control and monitoring and remedy performance monitoring and reviews, including National Emergency Rapid Response.
- Logistics – Leidos is a global leader in large-scale, complex operations and logistics. Our programs extend from the bottom of the world on the Antarctic ice to the orbiting outpost that is the International Space Station. Our expertise goes beyond supply sourcing, shipping, warehousing and maintenance as we also provide systems engineering, specialized product support, training and field readiness, base operations, data analytics and software development. We are helping our customers, including the United Kingdom Ministry of Defence ("U.K. MoD"), the National Science Foundation ("NSF") and the National Aeronautics and Space Administration ("NASA"), streamline logistics through data analytics so more of their budgets can be applied to their mission activities.

Health

Our Health business is focused on delivering effective and affordable solutions to federal and commercial customers that are responsible for the health and well-being of people worldwide including service members and veterans. Our solutions enable customers to deliver on the health mission of providing high quality, cost effective care, and are accomplished through the integration of information technology, engineering, health and life sciences, clinical insights and health policy. The capabilities we provide are principally encapsulated by four major areas of activity: complex systems integration, managed health services, enterprise IT transformation and life sciences. Health represented 18% of total revenues for fiscal 2018 and 2017 and 16% of total revenues for fiscal 2016.

- Complex Systems Integration – Leidos employs whole-systems thinking in fielding applied technology solutions across the entire continuum of care. We are working as the lead systems integrator deploying the next generation electronic health records system to DoD hospitals and treatment facilities worldwide, responsible for architecture, cyber and complex systems integration. We provide information technology solutions to the VA, National Institutes of Health, DoD and other government customers. Commercially, we are one of the largest systems integration and staff support firms for hospitals deploying modern electronic health records, and combined with our federal work, Leidos has a significant presence in electronic health record implementation, optimization and support. In addition, we provide consulting, platform integration services and support across a broad range of health operational activities including value based care enablement solutions, IT strategy, revenue cycle management, accountable care transformation, risk management, technology infrastructure and project management. Our teams are staffed with clinical subject matter experts who draw upon their deep experience and knowledge of healthcare and IT systems.

Table of Contents

- Managed Health Services – We deploy a national footprint of health clinics and health providers to support care delivery services, including medical disability examinations for the Veterans Administration (including behavioral assessments), as well as serving other independent medical exam markets. We have developed unique capabilities in behavioral health management through many decades of experience with a special emphasis on substance abuse services. Our managed health services activities leverage our IT and mission enablement capabilities which underpin solutions we offer to our customers across all of our served markets.
- Enterprise IT Transformation – We manage the entire lifecycle of the IT journey for our customers. Our expertise includes IT strategic planning, outsourcing and management of large scale data centers, agile software development and system transformation, cloud migration and application modernization, digitization and advanced analytics. Our customers include the Centers for Medicare & Medicaid Services, Food and Drug Administration, Social Security Administration, VA and commercial customers. Leidos helps transform our customers' IT environments in support of their most critical missions. All of this is accomplished in a highly secure manner by leveraging our cybersecurity capabilities.
- Life Sciences – We provide life science research and development support to the National Institutes of Health, Center for Disease Control, Army Medical Research community, commercial biotech companies and the Frederick National Laboratory for Cancer Research, where we employ approximately 2,300 scientists, technicians, administrators and support staff. Our professionals operate a wide range of leading-edge research and development laboratories in the areas of genetics and genomics, proteins and proteomics, advanced biomedical computing and information technology, biopharmaceutical development and manufacturing, nanotechnology characterization and clinical trials management.

From the biomedical sciences to implementing and optimizing electronic health records to enabling providers to perform care coordination and population health management, Leidos is pioneering the use of systems integration principles, processes and technologies to transform the health industry’s evolution towards better quality, more cost-effective and safe care.

Corporate

Corporate includes the operations of various corporate activities, certain expense items that are not reimbursed by our U.S. government customers and certain other expense items excluded from a reportable segment's performance.

Acquisitions and Divestitures

On August 16, 2016, a wholly-owned subsidiary of Leidos Holdings, Inc. merged with the Information Systems & Global Solutions business (the "IS&GS Business") of Lockheed Martin Corporation in a Reverse Morris Trust transaction. See "Management's Discussion and Analysis of Financial Condition and Results of Operations–Lockheed Martin Transaction" and "Note 6—Acquisitions" in Part II of this Annual Report on Form 10-K for a further description of the Lockheed Martin Transaction.

During fiscal 2016, we divested of our heavy construction business. For further information, see "Note 7—Divestitures" in Part II of this Annual Report on Form 10-K.

Key Customers

Substantially all of our revenues are generated in the United States. Our consolidated revenues are largely attributable to prime contracts or to subcontracts with other contractors engaged in work for the U.S. government, with the remaining attributable to international customers, including the U.K. MoD and Australian Department of Defense, and customers across a variety of commercial markets. Within the U.S. government, our revenues are diversified across many agencies, including various intelligence agencies, the U.S. Army, Navy and Air Force, DHS, FAA, TSA, the Defense Health Agency, VA, Department of Health and Human Services, NASA, NSF, the Environmental Protection Agency and research agencies such as the Defense Advanced Research Projects Agency.

Table of Contents
PART I

The percentage of total revenues for the U.S. government, its agencies and other customers comprising more than 10% of consolidated revenues for the periods presented were as follows:

	Year Ended December 28, 2018	December 29, 2017	December 30, 2016
U.S. Government	85%	84%	81%
U.S. DoD	47%	47%	56%
U.S. Army	13%	13%	14%

These customers have a number of subsidiary agencies that have separate budgets and procurement functions. Our contracts may be with the highest level of these agencies or with the subsidiary agencies of these customers.

Employees

As of December 28, 2018, we employed approximately 32,000 full and part-time employees in more than 30 countries worldwide. The experience and expertise of our employees makes Leidos capable of solving our customers' most challenging technical problems. Approximately 38% of our employees have degrees in science, technology, engineering or mathematics fields, nearly 1,000 employees have doctoral degrees, approximately 39% of our employees possess security clearances and approximately 22% of our employees are military veterans.

Research and Development

We conduct research and development activities under customer-funded contracts and with company-funded internal research and development ("IR&D") funds. IR&D efforts consist of projects involving basic research, applied research, development and systems and other concept formulation studies. IR&D expenses are included in selling, general and administrative expenses and are generally allocated to U.S. government contracts. For fiscal 2018, 2017 and 2016, our company-funded IR&D expense was $46 million, $42 million and $44 million, respectively, which as a percentage of consolidated revenues was 0.5%, 0.4% and 0.6%, respectively. We charge expenses for research and development activities performed under customer contracts directly to cost of revenues for those contracts.

Intellectual Property Rights

Our technical services and products are not generally dependent upon patent protection, although we do selectively seek patent protection. We claim a proprietary interest in certain of our products, software programs, methodologies and know-how. This proprietary information is protected in confidence as trade secrets, using non-disclosure agreements, contracts and other definitive agreements. We selectively pursue opportunities to license or transfer our technologies to third parties.

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

Competition

Competition for contracts is significant, and we often compete against a large number of well established corporations that may have greater name and brand recognition. We also compete against smaller, more specialized companies that concentrate their resources on particular areas, as well as the U.S. government’s own capabilities and federal non-profit contract research centers. As a result of the diverse requirements of the U.S. government and our commercial customers, we frequently collaborate with other companies to compete for large contracts and bid against these same companies in other situations.

Table of Contents

We believe that our principal competitors currently include the following companies: BAE Systems plc, Booz Allen Hamilton Inc., CACI International Inc., General Dynamics Corporation, L3 Technologies, Lockheed Martin Corporation, ManTech International Corporation, Northrop Grumman Corporation, Perspecta Inc., Raytheon Company and SAIC. These companies span across sectors that include engineering and technical services divisions of large defense contractors, diversified U.S. and international IT providers and contractors focused solely on technical services, supply chain management, other logistics services and major systems operations and maintenance, homeland security and health solutions.

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

The U.S. government has indicated that it intends to increase competition for future procurement of products and services, which has led to fewer sole source awards and more emphasis on cost-competitiveness and affordability. The U.S. government is also committed to maintaining a socioeconomically diverse base of suppliers, which may lead to contracts being set aside for smaller businesses. In addition, procurement initiatives to improve efficiency, refocus priorities and enhance best practices could result in fewer new opportunities for our industry as a whole, which would intensify competition within the industry as companies compete for a more limited set of new programs.

Contract Procurement

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

- Definitive Award Contracts. U.S. government agencies may procure services and products through single definitive award contracts which specify the scope of services or products purchased and identify the contractor that will provide the specified services or products. When an agency has a requirement, the agency will issue a solicitation or request for proposal to which interested contractors can submit a proposal. The bidding and selection process can take a year or more to complete. For the contractor, this method of contracting may provide greater certainty of the timing and amounts to be received at the time of contract award because it generally results in the customer contracting for a specific scope of services or products from the single definitive successful awardee.
- Indefinite Delivery/Indefinite Quantity ("IDIQ") Contracts. The U.S. government uses IDIQ contracts to obtain commitments from contractors to provide certain services or products on pre-established terms and conditions. The U.S. government then issues task orders under the IDIQ contracts to purchase the specific services or products it needs. IDIQ contracts are awarded to one or more contractors following a competitive procurement process. Under a single-award IDIQ contract, all task orders under that contract are awarded to one pre-established contractor. Under a multiple-award IDIQ contract, task orders can be awarded to any of the pre-established contractors, which can result in further limited competition for the award of task orders. Multiple-award IDIQ contracts that are open for any government agency to use for procurement are commonly referred to as "government-wide acquisition contracts." IDIQ contracts often have multi-year terms and unfunded ceiling amounts, therefore enabling, but not committing, the U.S. government to purchase substantial amounts of services or products from one or more contractors. At the time an IDIQ contract is awarded (prior to the award of any task orders), a contractor may have limited or no visibility as to the ultimate amount of services or products that the U.S. government will purchase under the contract, and in the case of a multiple-award IDIQ, the contractor from which such purchases may be made.

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

We often partner with other companies, including our competitors, to submit bids for large U.S. government procurements or other opportunities where we believe that the combination of services and products that we can provide as a team will help us win and perform the contract. Our relationships with our partners, including whether we serve as the prime contractor or as a subcontractor, vary with each contract opportunity and typically depend on the program, contract or customer requirements, as well as the relative size, qualifications, capabilities, customer relationships and experience of our company and our partners.

Contracting with the U.S. government also subjects us to substantial regulation and unique risks, including the U.S. government's ability to cancel any contract at any time through a termination for the convenience of the U.S. government. Most of our contracts have cancellation terms that would permit us to recover all or a portion of our incurred costs and fees for work performed where the U.S. government issues a termination for convenience. These regulations and risks are described in more detail below under "Business–Regulation" and "Risk Factors" in this Annual Report on Form 10-K.

Contract Types

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

- Cost-reimbursement contracts include cost-plus-fixed-fee, award-fee and incentive-fee contracts. These contracts provide for reimbursement of our direct contract costs and allocable indirect costs, plus a fee. These contracts are generally used when uncertainties involved in contract performance do not permit costs to be estimated with sufficient accuracy to use a fixed-price contract. Cost-reimbursement contracts generally subject us to lower risk but generally require us to use our best efforts to accomplish the scope of the work within a specified time and budget. Award and incentive fees are generally based on performance criteria such as cost, schedule, quality and/or technical performance. Award fees are determined and earned based on customer evaluation of the company's performance against contractual criteria. Incentive fees that are based on cost provide for an initially negotiated fee to be adjusted later, typically using a formula to measure performance against the associated criteria, based on the relationship of total allowable costs to total target costs.
- Fixed-price-incentive-fee ("FP-IF") contracts are substantially similar to cost-plus-incentive-fee contracts except they require specified targets for cost and profit, price ceiling (but not a profit ceiling or floor) and profit adjustment formula. Under an FP-IF contract, the allowable costs incurred are eligible for reimbursement but are subject to a cost-share arrangement, which affects profitability. Generally, if our costs exceed the contract target cost or are not allowable under the applicable regulations, we may not be able to obtain reimbursement for all costs and may have our fees reduced or eliminated.

Table of Contents

- Time-and-materials ("T&M") contracts typically provide for negotiated fixed hourly rates for specified categories of direct labor plus reimbursement of other direct costs. This type of contract is generally used when there is uncertainty about the extent or duration of the work to be performed by the contractor at the time of contract award or it is not possible to anticipate costs with any reasonable degree of confidence. On T&M contracts, we assume the risk of providing appropriately qualified staff to perform these contracts at the hourly rates set forth in the contracts over the period of performance of the contracts.
- Fixed-price-level-of-effort ("FP-LOE") contracts are substantially similar to T&M contracts except they require a specified level of effort over a stated period of time on work that can be stated only in general terms. This type of contract is generally used when the contractor is required to perform an investigation or study in a specific research and development area and to provide a report showing the results achieved based on the level of effort. Payment is based on the effort expended rather than the results achieved.
- Firm-fixed-price ("FFP") contracts provide for a fixed price for specified products, systems and/or services. This type of contract is generally used when the government acquires products and services on the basis of reasonably definitive specifications and which have a determinable fair and reasonable price. These contracts offer us potential increased profits if we can complete the work at lower costs than planned. While FFP contracts allow us to benefit from cost savings, these contracts also increase our exposure to the risk of cost overruns.

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

Backlog

Backlog represents the estimated amount of future revenues to be recognized under negotiated contracts as work is performed. Our backlog consists of funded backlog and negotiated unfunded backlog. Backlog includes priced option periods not yet exercised. We expect to recognize a substantial portion of our funded backlog from U.S. government customers as revenues within the next 12 months. However, the U.S. government may cancel any contract at any time through a termination for the convenience of the U.S. government. In addition, certain contracts with commercial or non-U.S. federal government customers included in funded backlog may include provisions that allow the customer to cancel at any time. Many of our contracts have cancellation terms that would permit us to recover all or a portion of our incurred costs and fees for work performed. For additional discussion and analysis of backlog, see "Results of Operations—Bookings and Backlog" in "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Part II of this Annual Report on Form 10-K.

Seasonality

The U.S. government's fiscal year ends on September 30 of each year. While not certain, it is not uncommon for U.S. government agencies to award extra tasks or complete other contract actions in the timeframe leading up to the end of its fiscal year in order to avoid the loss of unexpended fiscal year funds, which may favorably impact our third fiscal quarter. In addition, our quarterly results may be impacted by the number of working days in a given quarter. We tend to generate less revenue from our labor services during the fourth quarter as a result of the holiday season. For selected quarterly financial data, see "Selected Quarterly Financial Data" in Part II of this Annual Report on Form 10-K.

Table of Contents

Regulation

We are heavily regulated in most of the fields in which we operate. We provide services and products to numerous U.S. government agencies and entities, including to the DoD, the U.S. Intelligence Community and the DHS. When working with these and other U.S. government agencies and entities, we must comply with various laws and regulations relating to the formation, administration and performance of contracts. U.S. government contracts generally are subject to the Federal Acquisition Regulation ("FAR"), which sets forth policies, procedures and requirements for the acquisition of goods and services by the U.S. government, agency-specific regulations that implement or supplement the FAR, such as the Department of Defense Federal Acquisition Regulation Supplement, and other applicable laws and regulations. These regulations impose a broad range of requirements, many of which are unique to government contracting, including various procurement, import and export, security, contract pricing and cost, contract termination and adjustment and audit requirements. Among other things, these laws and regulations:

- require certification and disclosure of all cost and pricing data in connection with certain contract negotiations;
- define allowable and unallowable costs and otherwise govern our right to reimbursement under various cost-type U.S. government contracts;
- require compliance with U.S. government Cost Accounting Standards ("CAS");
- require reviews by the Defense Contract Audit Agency ("DCAA"), Defense Contract Management Agency ("DCMA") and other U.S. government agencies of compliance with government requirements for a contractor’s business systems;
- restrict the use and dissemination of and require the protection of unclassified contract-related information and information classified for national security purposes and the export of certain products and technical data; and
- require us not to compete for work if an actual or potential organizational conflict of interest, as defined by these laws and regulations, related to such work exists and/or cannot be appropriately mitigated, neutralized or avoided.

The U.S. government may revise its procurement practices or adopt new contract rules and regulations at any time. In order to help ensure compliance with these complex laws and regulations, all of our employees are required to complete ethics and other compliance trainings relevant to their position.

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

Environmental Matters

Our operations are subject to various foreign, federal, state and local environmental protection and health and safety laws and regulations. In addition, our operations may become subject to future laws and regulations, including those related to climate change and environmental sustainability. See "Risk Factors" in this Annual Report on Form 10-K for further details. Although we do not currently anticipate that the costs of complying with, or the liabilities associated with, environmental laws will materially and adversely affect us, we cannot ensure that we will not incur material costs or liabilities in the future.

Company Website and Information

Our website can be accessed at www.leidos.com. The website contains information about our company and operations. Through a link on the Investor Relations section of our website, copies of each of our filings with the U.S. Securities and Exchange Commission ("SEC") on Form 10-K, Form 10-Q and Form 8-K, and all amendments to those reports, can be viewed and downloaded free of charge as soon as reasonably practicable after the reports and amendments are electronically filed with or furnished to the SEC. The information on our website is not incorporated by reference into and is not a part of this Annual Report on Form 10-K.

Table of Contents

You may request a copy of the materials identified in the preceding paragraph, at no cost, by writing or telephoning us at our corporate headquarters at the following:

Leidos Holdings, Inc.
11951 Freedom Drive
Reston, VA 20190
Attention: Corporate Secretary
Telephone: (571) 526-6000

Table of Contents
PART I

Item 1A. Risk Factors
In your evaluation of our company and business, you should carefully consider the risks and uncertainties described below, together with information included elsewhere in this Annual Report on Form 10-K and other documents we file with the SEC. The risks and uncertainties described below are those that we have identified as material but are not the only risks and uncertainties facing us. If any of these risks or uncertainties actually occurs, our business, financial condition or operating results could be materially harmed and the price of our stock could decline. Our business is also subject to general risks and uncertainties that affect many other companies, such as our ability to collect receivables, overall U.S. and global economic and industry conditions, geopolitical events, changes in laws or accounting rules, fluctuations in interest and exchange rates, terrorism, international conflicts, major health concerns, climate change or other disruptions of expected economic and business conditions. Additional risks and uncertainties not currently known to us or that we currently believe are immaterial also may materially harm our business, financial condition or operating results and result in a decline in the price of our stock.
Risks Relating to Our Business
We depend on government agencies as our primary customer and if our reputation or relationships with these agencies were harmed, our future revenues and growth prospects would be adversely affected.
We generated 85%, 84% and 81% of our total revenues during fiscal 2018, 2017 and 2016, respectively, from contracts with the U.S. government (including all branches of the U.S. military), either as a prime contractor or a subcontractor to other contractors engaged in work for the U.S. government. We generated more than 10% of our total revenues during fiscal 2018, 2017 and 2016 from the U.S. Army. We expect to continue to derive most of our revenues from work performed under U.S. government contracts. Our reputation and relationship with the U.S. government, and in particular with the agencies of the DoD and the U.S. Intelligence Community, are key factors in maintaining and growing our revenues. Negative press reports or publicity, which could pertain to employee or subcontractor misconduct; conflicts of interest; poor contract performance; deficiencies in services, reports, products or other deliverables; information security breaches or other aspects of our business, regardless of accuracy, could harm our reputation, particularly with these agencies. If our reputation is negatively affected, or if we are suspended or debarred from contracting with government agencies for any reason, the amount of business with government and other customers would decrease and our future revenues and growth prospects would be adversely affected.
A decline in the U.S. government budget, changes in spending or budgetary priorities or delays in contract awards may significantly and adversely affect our future revenues and limit our growth prospects.
Revenues under contracts with the DoD, either as a prime contractor or subcontractor to other contractors, represented approximately 47% of our total revenues for fiscal 2018 and 2017 and 56% of our total revenues for fiscal 2016. Levels of U.S. government and DoD spending are difficult to predict and subject to significant risk. Our operating results could be adversely affected by spending caps or changes in the budgetary priorities of the U.S. government or the DoD, as well as delays in program starts or the award of contracts or task orders under contracts. Current U.S. government spending levels for defense-related or other programs may not be sustained and future spending and program authorizations may not increase or may decrease or shift to programs in areas in which we do not provide services or are less likely to be awarded contracts. Such changes in spending authorizations and budgetary priorities may occur as a result of uncertainty surrounding the federal budget, increasing political pressure and legislation, shifts in spending priorities from defense-related or other programs as a result of competing demands for federal funds, the number and intensity of military conflicts or other factors.
The U.S. government also conducts periodic reviews of U.S. defense strategies and priorities, which may shift DoD or other budgetary priorities, reduce overall U.S. government spending or delay contract or task order awards for defense-related or other programs, including programs from which we expect to derive a significant portion of our future revenues. In addition, changes to the federal or DoD acquisition system and contracting models could affect whether and how we pursue certain opportunities and the terms under which we are able to do so. A significant decline in overall U.S. government spending, including in the areas of national security, intelligence and homeland security, a significant shift in its spending priorities, the substantial reduction or elimination of particular

defense-related programs or significant delays in contract or task order awards for large programs could adversely affect our future revenues and limit our growth prospects.

Table of Contents

Because we depend on U.S. government contracts, a delay in the completion of the U.S. government's budget and appropriation process could delay procurement of the products, services and solutions we provide and have an adverse effect on our future revenues.

The funding of U.S. government programs is subject to an annual congressional budget authorization and appropriations process. In years when the U.S. government does not complete its appropriations before the beginning of the new fiscal year on October 1, government operations are typically funded pursuant to a "continuing resolution," which allows federal government agencies to operate at spending levels approved in the previous appropriations cycle, but does not authorize new spending initiatives. When the U.S. government operates under a continuing resolution, delays can occur in the procurement of the products, services and solutions that we provide and may result in new initiatives being canceled. We have from time to time experienced a decline in revenues in our fourth quarter as a result of this annual appropriations cycle, and we could experience similar declines in revenues from future delays in the appropriations process. When the U.S. government fails to complete its appropriations process or to provide for a continuing resolution, a full or partial federal government shutdown may result. A federal government shutdown could, in turn, result in our incurrence of substantial labor or other costs without reimbursement under customer contracts, the delay or cancellation of key programs or the delay of contract payments, which could have a negative effect on our cash flows and adversely affect our future results. In addition, when supplemental appropriations are required to operate the U.S. government or fund specific programs and passage of legislation needed to approve any supplemental appropriations bill is delayed, the overall funding environment for our business could be adversely affected. For additional discussion and analysis of the potential of an ongoing U.S. government shutdown, see "Business Environment and Trends" in "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Part II of this Annual Report on Form 10-K.

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

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

- the FAR and supplements, which regulate the formation, administration and performance of U.S. government contracts;
- the Truth in Negotiations Act, which requires certification and disclosure of cost and pricing data in connection with certain contract negotiations;
- the Procurement Integrity Act, which regulates access to competitor bid and proposal information and government source selection information and our ability to provide compensation to certain former government officials;
- the Civil False Claims Act, which provides for substantial civil penalties for violations, including for submission of a false or fraudulent claim to the U.S. government for payment or approval; and
- the U.S. government CAS, which imposes accounting requirements that govern our right to reimbursement under certain cost-based U.S. government contracts.

The FAR and many of our U.S. government contracts contain organizational conflict of interest clauses that may limit our ability to compete for or perform certain other contracts or other types of services for particular customers. Organizational conflicts of interest arise when we engage in activities that may make us unable to render impartial assistance or advice to the U.S. government, impair our objectivity in performing contract work or provide us with an unfair competitive advantage. A conflict of interest issue that precludes our competition for or performance on a significant program or contract could harm our prospects.

Table of Contents

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

Our industry has experienced, and we expect it will continue to experience, significant changes to business practices as a result of an increased focus on affordability, efficiencies and recovery of costs, among other items. U.S. government agencies may face restrictions or pressure regarding the type and amount of services that they may obtain from private contractors. Legislation, regulations and initiatives dealing with procurement reform, mitigation of potential conflicts of interest and environmental responsibility or sustainability, as well as any resulting shifts in the buying practices of U.S. government agencies, such as increased usage of fixed-price contracts, multiple-award contracts and small business set-aside contracts, could have adverse effects on government contractors, including us. Any of these changes could impair our ability to obtain new contracts or renew our existing contracts when those contracts are recompeted. Any new contracting requirements or procurement methods could be costly or administratively difficult for us to implement and could adversely affect our future revenues, profitability and prospects.

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

U.S. government agencies, including the DCAA, DCMA and others, routinely audit and review a contractor's performance on government contracts, indirect rates and pricing practices and compliance with applicable contracting and procurement laws, regulations and standards. They also review the adequacy of the contractor’s compliance with government standards for its business systems, including; a contractor's accounting system, earned value management system, estimating system, materials management and accounting system, property management system and purchasing system.

Both contractors and the U.S. government agencies conducting these audits and reviews have come under increased scrutiny. As a result, the current audits and reviews have become more rigorous and the standards to which we are held are being more strictly interpreted, increasing the likelihood of an audit or review resulting in an adverse outcome. During the course of its current audits, the DCAA is closely examining and questioning several of our long established and disclosed practices that it had previously audited and accepted, increasing the uncertainty as to the ultimate conclusion that will be reached.

A finding of significant control deficiencies in our system audits or other reviews can result in decremented billing rates to our U.S. government customers until the control deficiencies are corrected and our remediations are accepted by DCMA. Government audits and reviews may conclude that our practices are not consistent with applicable laws and regulations and result in adjustments to contract costs and mandatory customer refunds. Such adjustments can be applied retroactively, which could result in significant customer refunds. Our receipt of adverse audit findings or the failure to obtain an "approved" determination of our various business systems from the responsible U.S. government agency could significantly and adversely affect our business, including our ability to bid on new contracts and our competitive position in the bidding process. A determination of non-compliance with applicable contracting and procurement laws, regulations and standards could also result in the U.S. government imposing penalties and sanctions against us, including withholding of payments, suspension of payments and increased government scrutiny that could delay or adversely affect our ability to invoice and receive timely payment on contracts, perform contracts or compete for contracts with the U.S. government.

As of December 28, 2018, indirect cost audits by the DCAA remain open for fiscal 2013 and subsequent fiscal years. Although we have recorded contract revenues based upon our estimate of costs that we believe will be approved upon final audit or review, we cannot predict the outcome of any ongoing or future audits or reviews and adjustments and, if future adjustments exceed our estimates, our profitability may be adversely affected.

Table of Contents

Our business is subject to governmental review and investigation which could adversely affect our financial position, operating results and growth prospects.

We are routinely subject to governmental investigations relating to compliance with various laws and regulations with respect to our role as a contractor to federal, state and local government customers and in connection with performing services in countries outside the United States. If a review or investigation identifies improper or illegal activities, we may be subject to civil or criminal penalties or administrative sanctions, including the termination of contracts, forfeiture of profits, the triggering of price reduction clauses, suspension of payments, fines and suspension or debarment from doing business with governmental agencies. We may suffer harm to our reputation if allegations of impropriety are made against us, which would impair our ability to win new contract awards or receive contract renewals. Penalties and sanctions are not uncommon in our industry. If we incur a material penalty or administrative sanction or otherwise suffer harm to our reputation, our revenues, profitability, cash position and future prospects could be adversely affected. More generally, increases in scrutiny and investigations from government organizations, legislative bodies or agencies into business practices and into major programs supported by contractors may lead to increased legal costs and may harm our reputation, revenues, profitability and growth prospects.

Misconduct of employees, subcontractors, agents and business partners could cause us to lose existing contracts or customers and adversely affect our ability to obtain new contracts and customers and could have a significant adverse impact on our business and reputation.

Misconduct could include fraud or other improper activities such as falsifying time or other records and violations of laws, including the Anti-Kickback Act. Other examples could include the failure to comply with our policies and procedures or with federal, state or local government procurement regulations; regulations regarding the use and safeguarding of classified or other protected information; legislation regarding the pricing of labor and other costs in government contracts, laws and regulations relating to environmental, health or safety matters; bribery of foreign government officials; import-export control; lobbying or similar activities and any other applicable laws or regulations. Any data loss or information security lapses resulting in the compromise of personal information or the improper use or disclosure of sensitive or classified information could result in claims, remediation costs, regulatory sanctions against us, loss of current and future contracts and serious harm to our reputation. Although we have implemented policies, procedures and controls to prevent and detect these activities, these precautions may not prevent all misconduct, and as a result, we could face unknown risks or losses. Our failure to comply with applicable laws or regulations or misconduct by any of our employees, subcontractors, agents or business partners could damage our reputation and subject us to fines and penalties, restitution or other damages, loss of security clearance, loss of current and future customer contracts and suspension or debarment from contracting with federal, state or local government agencies, any of which would adversely affect our business, reputation and our future results.

Due to the competitive process to obtain contracts and the likelihood of bid protests, we may be unable to achieve or sustain revenue growth and profitability.

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

The U.S. government may terminate, cancel, modify or curtail our contracts at any time prior to their completion and, if we do not replace them, this may adversely affect our future revenues and profitability.

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

We have experienced and continue to experience periodic performance issues under certain of our contracts. Some of our contracts involve the development of complex systems and products to achieve challenging customer goals in a competitive procurement environment. As a result, we sometimes experience technological or other performance difficulties, which have in the past and may in the future result in delays, cost overruns and failures in our performance of these contracts. If a government customer terminates a contract for default, we may be exposed to liability, including for excess costs incurred by the customer in procuring undelivered services and products from another source. Depending on the nature and value of the contract, a performance issue or termination for default could cause our actual results to differ from those anticipated and could harm our reputation.

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

Our business is highly competitive and we compete with larger companies that have greater name recognition, financial resources and a larger technical staff. We also compete with smaller, more specialized companies that are able to concentrate their resources on particular areas. Additionally, we compete with the U.S. government's own capabilities and federal non-profit contract research centers.

The markets in which we operate are characterized by rapidly changing technology and the needs of our customers change and evolve regularly. Accordingly, our success depends on our ability to develop services and products that address these changing needs and to provide people and technology needed to deliver these services and products. To remain competitive, we must consistently provide superior service, technology and performance on a cost-effective basis to our customers. Our competitors may be able to provide our customers with different or greater capabilities or technologies or better contract terms than we can provide, including technical qualifications, past contract experience, geographic presence, price and the availability of qualified professional personnel. In addition, our competitors may consolidate or establish teaming or other relationships among themselves or with third parties to increase their ability to address customers' needs. Accordingly, we anticipate that larger or new competitors or alliances among competitors may emerge, which may adversely affect our ability to compete.

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

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

In addition to attracting and retaining qualified engineering, technical and professional personnel, we believe that our success will also depend on the continued employment of a highly qualified and experienced senior management team and its ability to retain existing business and generate new business. Our senior management team is important to our business because personal reputations and individual business relationships are a critical element of retaining and obtaining customer contracts in our industry, particularly with agencies performing classified operations. An inability to retain appropriately qualified and experienced senior executives could cause us to lose customers or new business opportunities.

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

As of December 28, 2018, our total backlog was $20.8 billion, including $6.4 billion in funded backlog. Due to the U.S. government's ability to not exercise contract options or to terminate, modify or curtail our programs or contracts and the rights of our non-U.S. government customers to cancel contracts and purchase orders in certain circumstances, we may realize less than expected or may never realize revenues from some of the contracts that are included in our backlog. Our unfunded backlog, in particular, contains management’s estimate of amounts expected to be realized on unfunded contract work that may never be realized as revenues. If we fail to realize as revenues amounts included in our backlog, our future revenues, profitability and growth prospects could be adversely affected.

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

We generate revenues under various types of contracts, which include cost-reimbursement, FP-IF, T&M, FP-LOE and FFP contracts. Our earnings and profitability may vary materially depending on changes in the proportionate amount of revenues derived from each type of contract, the nature of services or products provided, as well as the achievement of performance objectives and the stage of performance at which the right to receive fees, particularly under incentive-fee and award-fee contracts, is finally determined. Cost-reimbursement and T&M contracts are generally less profitable than FFP contracts. Our operating results in any period may also be affected, positively or negatively, by customers' variable purchasing patterns of our more profitable proprietary products.

Our profitability is adversely affected when we incur contract costs that we cannot bill to our customers. To varying degrees, each of our contract types involves some risk that we could underestimate the costs and resources necessary to fulfill the contract. While FFP contracts allow us to benefit from cost savings, these contracts also increase our exposure to the risk of cost overruns. Revenues from FFP contracts represented approximately 31% of our total revenues for fiscal 2018. When making proposals on these types of contracts, we rely heavily on our estimates of costs and timing to complete the associated projects, as well as assumptions regarding technical issues. In each case, our failure to accurately estimate costs or the resources and technology needed to perform our contracts or to effectively manage and control our costs during performance could result, and in some instances has resulted, in reduced profits or in losses. More generally, any increased or unexpected costs or unanticipated delays in the performance of our contracts, including costs and delays caused by contractual disputes or other factors outside of our control, such as performance failures of our subcontractors, natural disasters or other force majeure events, could make our contracts less profitable than expected or unprofitable.

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

We recognize revenue on our service based contracts primarily over time as there is continuous transfer of control to the customer over the duration of the contract as we perform the promised services, which generally requires estimates of total costs at completion, fees earned on the contract, or both. This estimation process, particularly due to the technical nature of the services performed and the long-term nature of certain contracts, is complex and involves significant judgment. Adjustments to original estimates are often required as work progresses, experience is gained and additional information becomes known, even though the scope of the work required under the contract may not change. Any adjustment as a result of a change in estimate is recognized as events become known. Changes in the underlying assumptions, circumstances or estimates could result in adjustments that may adversely affect our future financial results.

Table of Contents

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

We are subject to a number of lawsuits and claims described in "Legal Proceedings" in Part I of this Annual Report on Form 10-K, as may be updated in our future filings with the SEC, including our Quarterly Reports on Form 10-Q. We are also subject to, and may become a party to, a variety of other litigation or claims and suits that arise from time to time in the ordinary course of our business. Adverse judgments or settlements in some or all of these legal disputes may result in significant monetary damages, penalties or injunctive relief against us. Any claims or litigation could be costly to defend, and even if we are successful or if fully indemnified or insured, could damage our reputation and make it more difficult to compete effectively or obtain adequate insurance in the future. Litigation and other claims, including those described in "Legal Proceedings," are subject to inherent uncertainties and management's view of these matters may change in the future.

Our business and operations expose us to numerous legal and regulatory requirements, and any violation of these requirements could harm our business.

We are subject to numerous federal, state and foreign legal requirements on matters as diverse as data privacy and protection, employment and labor relations, immigration, taxation, anticorruption, import-export controls, trade restrictions, internal and disclosure control obligations, securities regulation and anti-competition. Compliance with diverse and changing legal requirements is costly, time-consuming and requires significant resources. We also conduct business in certain identified growth areas, such as health information technology, energy and environmental services, which are highly regulated and may expose us to increased compliance risk. Violations of one or more of these diverse legal requirements in the conduct of our business could result in significant fines and other damages, criminal sanctions against us or our officers, prohibitions on doing business and damage to our reputation. Violations of these regulations or contractual obligations related to regulatory compliance in connection with the performance of customer contracts could also result in liability for significant monetary damages, fines and/or criminal prosecution, unfavorable publicity and other reputational damage, restrictions on our ability to compete for certain work and allegations by our customers that we have not performed our contractual obligations.

Information security incidents could negatively impact our business and financial results or cause harm to our reputation or competitive position.

As a government contractor and a provider of information technology services operating in multiple regulated industries and geographies, we and our suppliers and subcontractors process and/or store sensitive information, including personally identifiable information, protected health information, personnel information, classified information, contractor unclassified information and financial information, concerning our business, employees and our customers. Therefore, we are continuously exposed to unauthorized attempts to compromise such sensitive information through cyber-attacks, insider threats and other information security threats, including physical break-ins and malicious insiders. Any electronic or physical break-in or other security breach or compromise may jeopardize security of information stored or transmitted through our information technology systems and networks. This could lead to disruptions in mission-critical systems, unauthorized release of confidential or otherwise protected information and corruption of data or systems.

Although we have implemented policies, procedures and controls to protect against, detect and mitigate these threats, we face advanced and persistent attacks on our information systems. Attempts by others to gain unauthorized access to sensitive information are constantly evolving, increasingly sophisticated and increasingly difficult to detect and successfully defend against. These attempts include covertly introducing malware to our computers and networks and impersonating authorized users, among others, and may be perpetrated by well-funded organized crime or state-sponsored efforts.

We seek to detect and investigate all information security incidents and to prevent their occurrence or recurrence. We continue to invest in and improve our threat protection, detection and mitigation policies, procedures and controls. In addition, we work with other companies in the industry and government participants on increased awareness and enhanced protections against information security and malicious insider threats. However, because of the evolving nature and sophistication of these security threats, which can be difficult to detect, there can be no assurance that our policies, procedures and controls have detected or will detect or prevent any of these threats and we cannot predict the full impact of any such past or future incident. We may be currently unaware of certain vulnerabilities or lack the capability to detect them, which may allow them to persist in our IT environment over long periods of time.

We may experience similar security threats to the information technology systems that we develop, install or maintain under customer contracts. Although we work cooperatively with our customers and other business partners, including our suppliers and subcontractors, to seek to minimize the impact of cyber and other security threats, we must rely on the safeguards put in place by those entities. Any remedial costs or other liabilities related to cyber or other security threats may not be fully insured or indemnified by other means. Occurrence of any of these security threats could disrupt our systems or those of our customers, impair our ability to provide services to our customers, result in product development delays, compromise confidential or technical business information and, as a result, expose us to claims, contract terminations and damages and could adversely affect our reputation, ability to win work on sensitive U.S. government contracts, business operations and financial results.

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

Any system or service disruptions, including those caused by ongoing projects to improve our information technology systems and the delivery of services, whether through our shared services organization or outsourced services, if not anticipated and appropriately mitigated, could have a material adverse effect on our business including, among other things, an adverse effect on our ability to perform on contracts, bill our customers for work performed on our contracts, collect the amounts that have been billed and produce accurate financial statements in a timely manner. We are also subject to systems failures, including network, software or hardware failures, whether caused by us, third-party service providers, cybersecurity threats, malicious insiders, natural disasters, power shortages, terrorist attacks or other events, which could cause loss of data and interruptions or delays in our business, cause us to incur remediation costs, subject us to claims and damage our reputation. In addition, the failure or disruption of our communications could cause us to interrupt or suspend our operations or otherwise adversely affect our business. Our property and business interruption insurance may be inadequate to compensate us for all losses that may occur as a result of any system or operational failure or disruption and, as a result, our future results could be adversely affected.

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

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

Many of our contracts contain performance obligations that require innovative design capabilities, are technologically complex or are dependent upon factors not wholly within our control. Failure to meet these obligations could adversely affect our profitability and future prospects.

We design and develop technologically advanced and innovative products and services applied by our customers in a variety of environments. Problems and delays in development or delivery as a result of issues with respect to design, technology, licensing and patent rights, labor, learning curve assumptions or materials and components could prevent us from achieving contractual requirements.

In addition, our offerings cannot be tested and proven in all situations and are otherwise subject to unforeseen problems that could negatively affect revenue and profitability such as problems with quality and workmanship, country of origin, delivery of subcontractor components or services and unplanned degradation of product performance. Among the factors that may affect revenue and profits could be unforeseen costs and expenses not covered by insurance or indemnification from the customer, diversion of management focus in responding to unforeseen problems, loss of follow-on work, and, in the case of certain contracts, repayment to the government customer of contract costs and fee payments we previously received.

Table of Contents

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

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

We have made and continue to make acquisitions, investments, joint ventures and divestitures that involve numerous risks and uncertainties.

We selectively pursue strategic acquisitions, investments and joint ventures. These transactions require significant investment of time and resources and may disrupt our business and distract our management from other responsibilities. Even if successful, these transactions could reduce earnings for a number of reasons, including the amortization of intangible assets, impairment charges, acquired operations that are not yet profitable or the payment of additional consideration under earn-out arrangements if an acquisition performs better than expected. Acquisitions, investments and joint ventures pose many other risks that could adversely affect our reputation, operations or financial results, including:

- we may not be able to identify, compete effectively for or complete suitable acquisitions and investments at prices we consider attractive;
- we may not be able to accurately estimate the financial effect of acquisitions and investments on our business, and we may not realize anticipated synergies or acquisitions may not result in improved operating performance;
- we may encounter performance problems with acquired technologies, capabilities and products, particularly with respect to those that are still in development when acquired;
- we may have trouble retaining key employees and customers of an acquired business or otherwise integrating such businesses, such as incompatible accounting, information management or other control systems, which could result in unforeseen difficulties;
- we may assume material liabilities that were not identified as part of our due diligence or for which we are unable to receive a purchase price adjustment or reimbursement through indemnification;
- we may assume legal or regulatory risks, particularly with respect to smaller businesses that have immature business processes and compliance programs;
- acquired entities or joint ventures may not achieve expected business growth or operate profitably, which could adversely affect our operating income or operating margins, and we may be unable to recover investments in any such acquisitions;
- acquisitions, investments and joint ventures may require us to spend a significant amount of cash or to issue capital stock, resulting in dilution of ownership; and
- we may not be able to effectively influence the operations of our joint ventures, or we may be exposed to certain liabilities if our joint venture partners do not fulfill their obligations.

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

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

Goodwill and other intangible assets represent approximately 63% of our total assets and any impairment of these assets could negatively impact our results of operations.

Intangible assets with indefinite lives, including goodwill, are tested for impairment at least annually or whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Intangible assets with finite lives are assessed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Examples of events or changes in circumstances indicating that the carrying value of intangible assets may not be recoverable could include a significant adverse change in legal factors or in the business climate, an adverse action or assessment by a regulator, unanticipated competition, loss of key personnel, or a more-likely-than-not expectation that a reporting unit or a significant portion of a reporting unit will be sold or otherwise disposed. We face continued uncertainty in our business environment due to the substantial fiscal and economic challenges facing the U.S. government, our primary customer, as well as challenges in the commercial healthcare industry, compounded by lower levels of U.S. government reimbursements, including reductions in Medicare reimbursements which in turn impact hospital IT spending. Adverse changes in fiscal and economic conditions, such as the manner in which budget cuts are implemented, including sequestration, and issues related to the nation’s debt ceiling, could adversely impact our future revenues and profitability. These circumstances could result in an impairment of goodwill and/or other intangibles. Also, adverse equity market conditions that result in a decline in market multiples and our stock price could result in an impairment of goodwill and/or other intangibles. Any future impairment of goodwill or other intangible assets would have a negative impact on our profitability and financial results.

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

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

We may have disputes with our subcontractors arising from, among other things, the quality and timeliness of work performed by the subcontractor, customer concerns about the subcontractor, our failure to extend existing task orders or issue new task orders under a subcontract, our hiring of a subcontractor’s personnel or the subcontractor’s failure to comply with applicable law. Uncertain economic conditions heighten the risk of financial stress of our subcontractors, which could adversely impact their ability to meet their contractual requirements to us. If any of our subcontractors fail to timely meet their contractual obligations or have regulatory compliance or other problems, our ability to fulfill our obligations as a prime contractor or higher tier subcontractor may be jeopardized. Significant losses could arise in future periods and subcontractor performance deficiencies could result in our termination for default. A termination for default could eliminate a revenue source, expose us to liability and have an adverse effect on our ability to compete for future contracts and task orders, especially if the customer is an agency of the U.S. government.

Table of Contents

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

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

We could incur significant liabilities and suffer negative publicity if our inspection or detection systems fail to detect bombs, explosives, weapons, contraband or other threats.

We design, develop, manufacture, sell, service and maintain various inspection systems that are designed to assist in the detection of bombs, explosives, weapons, contraband or other threats. In some instances, we also train operators of such systems. Many of these systems utilize software algorithms that are probabilistic in nature and subject to significant technical limitations. Many of these systems are also dependent on the performance of their operators. There are many factors, some of which are beyond our control, which could result in the failure of our products to help detect the presence of bombs, explosives, weapons, contraband or other threats. Some of these factors could include operator error, inherent limitations in our systems and misuse or malfunction of our systems. The failure of our systems to help detect the presence of any of these dangerous materials could lead to injury, death and extensive property damage and may lead to product liability, professional liability or other claims against us. Further, if our systems fail to, or are perceived to have failed to help detect a threat, the negative publicity from such incident could have a material adverse effect on our business.

Our insurance may be insufficient to protect us from product and other liability claims or losses.

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

We face risks associated with our international business.

Our international business operations may be subject to additional and different risks than our U.S. business. Failure to comply with U.S. government and foreign laws and regulations applicable to international business, such as the Foreign Corrupt Practices Act or U.S. export control regulations, could have an adverse impact on our business with the U.S. government and could expose us to administrative, civil or criminal penalties. Additionally, these risks relating to international operations may expose us to potentially significant contract losses.

Table of Contents

In some countries, there is an increased chance for economic, legal or political changes that may adversely affect the performance of our services, sale of our products or repatriation of our profits. International transactions can also involve increased financial and legal risks arising from foreign exchange rate variability, imposition of tariffs or additional taxes, restrictive trade policies, any delay or failure to collect amounts due to us and differing legal systems. We provide services and products in support of U.S. government customers in countries with governments that may be or may become unstable, which increases the risk of an incident resulting in injury or loss of life, damage or destruction of property or inability to meet our contractual obligations. Although our international operations have historically generated a small proportion of our revenues, we are seeking to grow our international business, in which case these regulatory, geopolitical and other factors may have a greater impact on our business in the future and could adversely affect our business.

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

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

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

Our financial results may vary significantly from period-to-period.

Our financial results may fluctuate as a result of a number of factors, many of which are outside of our control. For these reasons, comparing our operating results on a period-to-period basis may not be meaningful, and you should not rely on our past results as an indication of our future performance. Our financial results may be negatively affected by any of the risk factors listed in this "Risk Factors" section and other matters described elsewhere in this Annual Report on Form 10-K.

We use estimates in accounting for many of our programs and changes in our estimates could adversely affect our future financial results.

Accounting for many of our programs requires judgment relative to assessing risks, including risks associated with estimating directed delays and reductions in scheduled deliveries, unfavorable resolutions of claims and contractual matters, judgments associated with estimating contract revenues and costs, and assumptions for schedule and technical issues. Due to the size and nature of many of our contracts, the estimation of total revenues and cost at completion is complicated and subject to many variables. For example, we must make assumptions regarding the length of time to complete the contract because costs also include expected increases in wages and prices for materials, consider whether the intent of entering into multiple contracts was effectively to enter into a single project in order to determine whether such contracts should be combined or segmented, consider incentives or penalties related to performance on contracts in estimating revenue and profit rates and record them when there is sufficient information for us to assess anticipated performance and use estimates of award fees in estimating revenue and profit rates based on actual and anticipated awards. Because of the significance of the judgments and estimation processes involved in accounting, materially different amounts could be recorded if we used different assumptions or if the underlying circumstances were to change. Changes in underlying assumptions, circumstances or estimates may adversely affect our future results of operations and financial condition.

Table of Contents
PART I

Risks Relating to Our Stock

We cannot assure you that we will continue to pay dividends on our common stock.

In March 2012, our Board of Directors approved the initiation of a quarterly dividend program. The timing, declaration, amount and payment of any future dividends fall within the discretion of our Board of Directors and will depend on many factors, including our available cash, estimated cash needs, earnings, financial condition, operating results and capital requirements, as well as limitations in our contractual agreements, applicable law, regulatory constraints, industry practice and other business considerations that our Board of Directors considers relevant. A change in our dividend program could have an adverse effect on the market price of our common stock.

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

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

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

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

Forward-Looking Statement Risks

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

This Annual Report on Form 10-K contains forward-looking statements that are based on our management's belief and assumptions about the future in light of information currently available to our management. In some cases, you can identify forward-looking statements by words such as "may," "will," "should," "expects," "intends," "plans," "anticipates," "believes," "estimates," "predicts," "potential," "continue," and similar words or phrases or the negative of these words or phrases. These statements relate to future events or our future financial performance, and involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements. Although we believe that the expectations reflected in the forward-looking statements are reasonable when made, we cannot guarantee future results, levels of activity, performance or achievements. There are a number of important factors that could cause our actual results to differ materially from those results anticipated by our forward-looking statements, which include, but are not limited to:

Leidos Holdings, Inc. Annual Report - 23

- developments in the U.S. government defense budget, including budget reductions, sequestration, implementation of spending limits or changes in budgetary priorities, or delays in the U.S. government budget process or approval of raising the debt ceiling;
- delays in the U.S. government contract procurement process or the award of contracts and delays or loss of contracts as a result of competitor protests;
- changes in U.S. government procurement rules, regulations and practices;
- our compliance with various U.S. government and other government procurement rules and regulations;
- governmental reviews, audits and investigations of our company;
- our ability to effectively compete and win contracts with the U.S. government and other customers;
- our reliance on information technology spending by hospitals/healthcare organizations;
- our reliance on infrastructure investments by industrial and natural resources organizations;
- energy efficiency and alternative energy sourcing investments;
- investments by U.S. government and commercial organizations in environment impact and remediation projects;
- our ability to attract, train and retain skilled employees, including our management team, and to obtain security clearances for our employees;
- our ability to accurately estimate costs associated with our FFP and other contracts;
- resolution of legal and other disputes with our customers and others or legal or regulatory compliance issues;
- cybersecurity, data security or other security threats, system failures or other disruptions of our business;
- our ability to effectively acquire businesses and make investments;
- our ability to maintain relationships with prime contractors, subcontractors and joint venture partners;
- our ability to manage performance and other risks related to customer contracts;
- the failure of our inspection or detection systems to detect threats;
- the adequacy of our insurance programs designed to protect us from significant product or other liability claims;
- our ability to manage risks associated with our international business;
- exposure to lawsuits and contingencies associated with Lockheed Martin’s IS&GS business;
- our ability to declare future dividends based on our earnings, financial condition, capital requirements and other factors, including compliance with applicable law and our agreements;
- our ability to grow our commercial health and infrastructure businesses, which could be negatively affected by budgetary constraints faced by hospitals and by developers of energy and infrastructure projects;
- for acquisitions that we agree to but are unable for regulatory or other reasons to consummate, we may incur break-up fees; and
- our ability to execute our business plan and long-term management initiatives effectively and to overcome these and other known and unknown risks that we face.

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

Item 1B. Unresolved Staff Comments

None.

Table of Contents
PART I

Item 2. Properties
As of December 28, 2018, we conducted our operations in 334 offices located in 37 states, the District of Columbia and various foreign countries. We occupy approximately 6.8 million square feet of floor space. Of this amount, we own approximately 0.9 million square feet, and the remaining balance is leased. Our major locations are in the Washington, D.C., metropolitan area, where we occupy a combination of leased and owned floor space of approximately 3.7 million square feet. We also have employees working at customer sites throughout the United States and in other countries.
As of December 28, 2018, we owned the following properties:

Location	Number of buildings	Square footage	Acreage
Gaithersburg, Maryland	1	542,000	44.8
Columbia, Maryland	1	95,000	7.3
Orlando, Florida	1	85,000	8.5
Oak Ridge, Tennessee	1	83,000	8.4
Reston, Virginia	1	62,000	2.6

The nature of our business is such that there is no practicable way to relate occupied space to our reportable segments. See "Note 27—Subsequent Events" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K for information regarding the sale of our Gaithersburg, Maryland property which occurred on December 31, 2018. See "Note 22—Leases" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K for information regarding commitments under leases.
Item 3. Legal Proceedings
We have provided information about legal proceedings in which we are involved in "Note 25—Contingencies" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K.
In addition, we are routinely subject to investigations and reviews relating to compliance with various laws and regulations. Additional information regarding such investigations and reviews is set forth in "Note 25—Contingencies" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K.
Item 4. Mine Safety Disclosures
Not applicable.
Executive Officers of the Registrant
The following is a list of the names and ages (as of February 19, 2019) of our executive officers, indicating all positions and offices held by each such person and each such person's business experience during at least the past five years. All such persons have been elected to serve until their successors are elected and qualified or until their earlier resignation or removal.

Name of officer	Age	Position(s) with the company and prior business experience
Roger A. Krone	62	Mr. Krone has served as Chief Executive Officer since July 2014. Mr. Krone is also Chairman of the Board. He brings more than 37 years of operational, strategic and financial execution experience for some of the nation's most prominent names in aerospace. Mr. Krone has held senior program management and finance positions at The Boeing Company, McDonnell Douglas Corp. and General Dynamics. Mr. Krone is currently a member of the Georgia Tech Foundation Board of Trustees. He is a long-time supporter of the Urban League and currently serves on the board of the Greater Washington chapter. He is also a member of the Executive Council of the Aerospace Industries Association and a member of the AOPA Foundation's Board of Visitors.

Name of officer	Age	Position(s) with the company and prior business experience
James C. Reagan	60	Mr. Reagan has served as Executive Vice President and Chief Financial Officer since July 2015. Prior to joining Leidos, from 2012 to 2015, Mr. Reagan was with Vencore, Inc. (formerly The SI Organization, Inc.), a provider of information solutions and engineering and analysis services to the U.S. Intelligence Community, DoD and federal and civilian agencies, where he served as Senior Vice President and Chief Financial Officer. From 2011 to 2012, Mr. Reagan was Executive Vice President and Chief Financial Officer of PAE, Inc., a provider of mission support services to the U.S. government. Mr. Reagan is a Certified Public Accountant.
Ranjit S. Chadha	48	Mr. Chadha has served as Senior Vice President, Chief Accounting Officer and Controller since April 2016, and before that, as Assistant Controller. Prior to joining Leidos, Mr. Chadha spent six years at CSC (now DXC), and during his tenure there held several roles with progressive responsibility, most recently as an Assistant Controller at CSC. Prior to CSC, he spent 17 years at PwC, including two years in the firm's National Office Assurance Quality Group. He is a Certified Public Accountant as well as a Chartered Accountant from India.
Paul O. Engola	47	Mr. Engola has served as Senior Vice President, Chief Human Resources Officer and Head of Business Partnerships since January 2019, and before that, as Chief Administrative Officer and Deputy President, Defense and Intelligence Group. Prior to joining Leidos, Mr. Engola served Lockheed Martin Corporation for more than 10 years, most recently as Vice President, Transportation & Financial Solutions in their former Information Systems & Global Solutions business.
Gerard A. Fasano	53	Mr. Fasano has served as Executive Vice President and President, Defense Group since October 2018, and before that, as Chief Business Development Strategy Officer. Prior to joining Leidos, Mr. Fasano served Lockheed Martin Corporation for over 30 years in several capacities, most recently as a Vice President and General Manager in their former Information Systems & Global Solutions business.
Angela L. Heise	44	Ms. Heise has served as President, Civil Group since August 2016 when she joined Leidos. Prior to joining Leidos, Ms. Heise served as Vice President of Commercial Cyber for Lockheed Martin Corporation's former Information Systems & Global Solutions business.
Jerald S. Howe, Jr.	63	Mr. Howe has served as Executive Vice President and General Counsel since July 2017. Prior to joining Leidos, Mr. Howe was a partner at Fried, Frank, Harris, Shriver & Jacobson LLP, where he served in the firm’s government contracts, mergers and acquisitions, and aerospace and defense practices. Prior to joining Fried Frank, Mr. Howe held general counsel positions at TASC, a leading aerospace and defense company, and at Veridian Corporation, a publicly traded company that provided advanced technology services and solutions to the intelligence community, military and homeland defense agencies.
Mary V. Schmanske	56	Ms. Schmanske has served as Senior Vice President and President, Intelligence Group since October 2018, and before that, as Chief Administrative Officer and Deputy President and Chief Operations Officer, Health Group. Prior to joining Leidos, Ms. Schmanske served Lockheed Martin Corporation in several capacities, most recently as Vice President of Operations for programs under strategic review, Civil, Defense & Intelligence Solutions.
Jonathan W. Scholl	57	Mr. Scholl has served as President, Health Group since August 2016, and before that, as President, Health and Infrastructure Group. Prior to joining Leidos, Mr. Scholl served for five years as the Chief Strategy Officer for Texas Health Resources, one of the largest nonprofit health care delivery systems in the country. Prior to that, he spent 15 years with The Boston Consulting group and served as head of their North American Healthcare Provider Practice and leader of their Lean Six Sigma initiative for hospitals. He also served as Vice President for Applications Development for

the TenFold HealthCare Group in Dallas. Mr. Scholl served five years in the U.S. Navy as a nuclear submarine officer and nuclear power plant instructor.

Table of Contents
PART II

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

Our common stock is listed on the New York Stock Exchange ("NYSE") under the ticker symbol "LDOS."

Holders of Common Stock

As of February 11, 2019, there were approximately 21,150 holders of record of Leidos common stock. The number of stockholders of record of our common stock is not representative of the number of beneficial owners due to the fact that many shares are held by depositories, brokers or nominees.

Dividend Policy

During fiscal 2018 and 2017, we declared and paid quarterly dividends totaling $1.28 per share of Leidos common stock. We currently intend to continue paying dividends on a quarterly basis, although the declaration of any future dividends will be determined by our Board of Directors and will depend on many factors, including available cash, estimated cash needs, earnings, financial condition, operating results and capital requirements, as well as limitations in our contractual agreements, applicable law, regulatory constraints, industry practice and other business considerations that the Board of Directors considers relevant. Our ability to declare and pay future dividends on Leidos stock may be restricted by the provisions of Delaware law and covenants in our then-existing indebtedness arrangements.

Table of Contents
PART II

Stock Performance Graph
The following graph compares the total cumulative five-year return on Leidos common stock through December 28, 2018 to two indices: (i) the Standard & Poor's 400 Composite index and (ii) the Standard & Poor's 500 IT Services Industry index. The graph assumes an initial investment of $100 on December 31, 2013, and that dividends, if any, have been reinvested.The comparisons in the graph are required by the SEC, based upon historical data and are not intended to forecast or be indicative of possible future performance of Leidos common stock.
Purchases of Equity Securities
On February 16, 2018, our Board of Directors authorized a new share repurchase program of up to 20 million shares of Leidos outstanding common stock. The shares may be repurchased from time to time in one or more open market repurchases or privately negotiated transactions, including accelerated share repurchase transactions. The actual timing, number and value of shares repurchased under the program will depend on a number of factors, including the market price of Leidos common stock, general market and economic conditions, applicable legal requirements, compliance with the terms of our outstanding indebtedness and other considerations. There is no assurance as to the number of shares that will be repurchased, and the repurchase program may be suspended or discontinued at any time at our Board of Directors' discretion. This share repurchase authorization replaced the previous share repurchase authorization announced in December 2013.

Table of Contents
PART II

The following table presents repurchases of Leidos common stock during the quarter ended December 28, 2018:

Period	Total Number of Shares Purchased[1]	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Repurchase Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
September 29, 2018 - September 30, 2018	—	$ —	—	17,535,284
October 1, 2018 - October 31, 2018[2]	3,347,602	63.18	3,345,876	14,189,408
November 1, 2018 - November 30, 2018	8,504	64.82	—	14,189,408
December 1, 2018 - December 28, 2018[2]	690,720	63.18	690,674	13,498,734
Total	4,046,826	$ 63.18	4,036,550	

(1) The total number of shares purchased includes shares surrendered to satisfy statutory tax withholdings obligations related to vesting of restricted stock units.

(2) In October 2018, we entered into an Accelerated Share Repurchase agreement with a financial institution, whereby we paid an aggregate of $250 million and received approximately 4.0 million shares of Leidos outstanding shares of common stock during the fourth quarter of fiscal 2018. All shares delivered were immediately retired. See "Note 18—Earnings Per Share" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K for further information.

Item 6. Selected Financial Data

The selected financial data for the five-year period set forth below is derived from our consolidated financial statements for fiscal years 2018, 2017 and 2016, the 11-month period ended January 1, 2016, and fiscal 2015. This information should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Part II and our consolidated financial statements and the notes thereto contained within this Annual Report on Form 10-K.

Table of Contents
PART II

	12 Months Ended[1]			11 Months Ended[1]	12 Months Ended[1]
	December 28, 2018[2]	December 29, 2017[3]	December 30, 2016[4]	January 1, 2016[5]	January 30, 2015[6]
	(in millions, except for per share amounts)				
Consolidated Statement of Income (Loss) Data:					
Revenues	$10,194	$ 10,170	$ 7,043	$ 4,712	$ 5,063
Operating income (loss)	749	559	417	320	(214)
Income (loss) from continuing operations	582	364	246	243	(330)
(Loss) income from discontinued operations, net of taxes	—	—	—	(1)	7
Net income (loss)	582	364	246	242	(323)
Less: net income (loss) attributable to non-controlling interest	1	(2)	2	—	—
Net income (loss) attributable to Leidos Holdings, Inc.	$581	$ 366	$ 244	$ 242	$ (323)
Earnings (loss) per share:					
Basic:					
Income (loss) from continuing operations attributable to Leidos common stockholders	$3.85	$ 2.41	$ 2.39	$ 3.33	$ (4.46)
(Loss) income from discontinued operations, net of taxes	—	—	—	(0.01)	0.10
Net income (loss) attributable to Leidos common stockholders	$3.85	$ 2.41	$ 2.39	$ 3.32	$ (4.36)
Diluted:					
Income (loss) from continuing operations attributable to Leidos common stockholders	$3.80	$ 2.38	$ 2.35	$ 3.28	$ (4.46)
(Loss) income from discontinued operations, net of taxes	—	—	—	(0.01)	0.10
Net income (loss) attributable to Leidos common stockholders	$3.80	$ 2.38	$ 2.35	$ 3.27	$ (4.36)
Cash dividend per common share	$1.28	$ 1.28	$ 14.92	$ 1.28	$ 1.28

	December 28, 2018	December 29, 2017	December 30, 2016	January 1, 2016	January 30, 2015
	(in millions)				
Consolidated Balance Sheet Data:					
Total assets	$8,770	$ 8,990	$ 9,132	$ 3,370	$ 3,281
Long-term debt, including current portion	3,124	3,111	3,287	1,081	1,158
Other long-term liabilities[7]	178	129	204	149	147

(1) References to financial data are to the Company's continuing operations, unless otherwise noted.

(2) Fiscal 2018 reflects the effects from our December 30, 2017 adoption of ASC 606. Fiscal 2018 also includes acquisition, integration and restructuring costs of $37 million and a tangible asset impairment charge of $7 million. For further information, see "Note 6—Acquisitions," "Note 8—Restructuring Expenses" and "Note 12—Property, Plant and Equipment" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K.

(3) Fiscal 2017 includes acquisition, integration and restructuring costs of $139 million. For further information, see "Note 6—Acquisitions" and "Note 8—Restructuring Expenses" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K.

(4) Fiscal 2016 includes acquisition, integration and restructuring costs of $104 million. For further detail regarding the acquisition of the IS&GS Business, see "Note 6—Acquisitions" and "Note 8—Restructuring Expenses" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K.

Table of Contents
PART II

(5) Reflects the 11-month period of January 31, 2015, through January 1, 2016, as a result of the change in our fiscal year end. The 11-month period ended January 1, 2016, results include a gain on a real estate sale of $82 million, tangible asset impairment charges of $29 million, intangible asset impairment charges of $4 million and bad debt expense of $8 million.

(6) Fiscal 2015 results include goodwill impairment charges of $486 million, intangible asset impairment charges of $41 million and a tangible asset impairment charge of $40 million.

(7) Beginning in fiscal 2016, the Company has separately disclosed "Deferred tax liabilities," which was previously aggregated within "Other long-term liabilities" within the consolidated balance sheets. Deferred tax liabilities for the 11-month period ended January 1, 2016 and fiscal 2015 were $34 million and $21 million, respectively.

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

The following discussion and analysis of Leidos Holdings, Inc.'s ("Leidos") financial condition, results of operations and quantitative and qualitative disclosures about market risk should be read in conjunction with the consolidated financial statements and related notes.

Unless indicated otherwise, references in this report to the "Company," "we," "us," and "our" refer collectively to Leidos and its consolidated subsidiaries.

The following discussion contains forward-looking statements, including statements regarding our intent, belief, or current expectations with respect to, among other things, trends affecting our financial condition or results of operations, backlog, initiatives, our industry and government budgets and spending. Such statements are not guarantees of future performance and involve risks and uncertainties, and actual results may differ materially from those in the forward-looking statements as a result of various factors (see "Risk Factors—Forward-Looking Statement Risks" in Part I of this Annual Report on Form 10-K). Factors that could cause or contribute to these differences include those discussed below and elsewhere in this Annual Report on Form 10-K, particularly in "Risk Factors" and "Business Environment and Trends." Due to such uncertainties and risks, you are cautioned not to place undue reliance on such forward-looking statements, which speak only as of the date hereof. We do not undertake any obligation to update these factors or to publicly announce the results of any changes to our forward-looking statements due to future events or developments.

Overview

We are a FORTUNE 500® science, engineering and information technology company that provides services and solutions in the defense, intelligence, civil and health markets. We bring domain-specific capability and cross-market innovations to customers in each of these markets by leveraging seven core capabilities: enterprise modernization; cyber operations; operations and logistics; mission software systems; integrated systems; sensors and phenomenology; and mission support. Our domestic customers include the U.S. Department of Defense ("DoD"), the U.S. Intelligence Community, the U.S. Department of Homeland Security, the Federal Aviation Administration, the Department of Veterans Affairs and many other U.S. government civilian agencies, as well as state and local government agencies. Our international customers include foreign governments and their agencies, primarily located in Australia and the United Kingdom ("U.K."). Less than 10% of our revenues and tangible long-lived assets are generated by or owned by entities located outside of the United States.

During fiscal 2017, we completed a business reorganization, which resulted in the identification of three reportable segments (Defense Solutions, Civil and Health). Additionally, we separately present the costs associated with corporate functions as Corporate. We commenced operating and reporting under the new organizational structure effective the beginning of fiscal 2017. As a result of this change, fiscal 2016 segment results and disclosures have been recast to reflect the new reportable segments.

For additional information regarding our reportable segments, see "Business" in Part I and "Note 24—Business Segments" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K.

Our significant initiatives include the following:

- achieving internal, or non-acquisition related, annual revenue growth through internal collaboration and better leveraging of key differentiators across our company and the deployment of resources and investments into higher growth markets;

- increasing headcount and internal direct labor content on our contract portfolio;
- continued improvement in our back office infrastructure and related business processes for greater effectiveness and efficiency across all business functions; and

- disciplined deployment of our cash resources and use of our capital structure to enhance shareholder value while retaining an appropriate amount of financial leverage, through internal growth initiatives, stock repurchases, dividends, strategic acquisitions, debt level management and other uses to achieve our goals.

Sales Trend. For fiscal 2018, revenues were $10.2 billion, consistent with fiscal 2017. For fiscal 2017, revenues increased by $3.1 billion, or 44%, compared to fiscal 2016, primarily attributable to the Information Systems & Global Solutions business (the "IS&GS Business") of Lockheed Martin Corporation acquired during the third quarter of fiscal 2016 and growth in airborne programs. The increase was partially offset by fiscal 2016 revenues from the divestiture of the heavy construction business, net volume decreases and lower revenues from our international business. See "Results of Operations" below for discussion of our individual segment results.

Operating Expenses and Income Trend. For fiscal 2018, operating expenses decreased by $161 million, or 2%, compared to fiscal 2017. Operating margin for fiscal 2018 was 7.3% compared to 5.5% for fiscal 2017. Operating income was $749 million for fiscal 2018, a $190 million increase compared to fiscal 2017. These changes were primarily attributable to decreases in acquisition, integration and restructuring costs and lower amortization of intangible assets.

For fiscal 2017, operating expenses increased by $3.0 billion, or 45%, compared to fiscal 2016, primarily attributable to the acquired IS&GS Business. Operating margin for fiscal 2017 was 5.5% compared to 5.9% for fiscal 2016. The decrease in operating margin was primarily due to a contract write-up in fiscal 2016 along with an increase in acquisition, integration and restructuring costs. For fiscal 2017, our operating income was $559 million, a $142 million increase compared to fiscal 2016. The increase in operating income was primarily attributable to the operating results of the acquired IS&GS Business.

From a macroeconomic perspective, our industry is under general competitive pressures associated with spending from our largest customer, the U.S. government, and has required and will require a higher level of cost management focus to allow us to remain competitive. Although the current Administration has indicated a desire to increase spending, primarily in the defense and homeland security sectors, the likelihood, extent and duration of higher spending in these areas remains unclear. We continue to review our cost structure against our anticipated sales and undertake cost management actions and efficiency initiatives where necessary.

Lockheed Martin Transaction

On January 26, 2016, Leidos announced that it had entered into a definitive agreement (as amended, the "Merger Agreement") with Lockheed Martin Corporation ("Lockheed Martin"); Abacus Innovations Corporation, a Delaware corporation and a wholly owned subsidiary of Lockheed Martin ("Splitco"); and Lion Merger Co., a Delaware corporation and, at the time of announcement, a wholly owned subsidiary of Leidos ("Merger Sub"), pursuant to which Leidos would combine with Lockheed Martin’s realigned Information Systems & Global Solutions business in a Reverse Morris Trust transaction. In connection with the Merger Agreement, Lockheed Martin and Splitco entered into a Separation Agreement dated January 26, 2016 (as amended, the "Separation Agreement"), pursuant to which Lockheed Martin would separate the IS&GS Business from Lockheed Martin and transfer the IS&GS Business to Splitco. The transactions contemplated by the Merger Agreement and the Separation Agreement are referred to herein as the "Transactions."

On August 16, 2016, the acquisition date, we completed the Transactions. In the Transactions, among other steps, (i) Lockheed Martin transferred the IS&GS Business to Splitco; (ii) Lockheed Martin offered to Lockheed Martin stockholders the right to exchange all or a portion of their shares of Lockheed Martin common stock for shares of Splitco common stock by way of an exchange offer (the "Distribution"); and (iii) Merger Sub merged with and into Splitco, with Splitco as the surviving corporation (the "Merger") and a wholly owned subsidiary of Leidos. Upon consummation of the Transactions, those Lockheed Martin stockholders who elected to participate in the exchange offer received approximately 77 million shares of Leidos common stock, which represented approximately 50.5% of the outstanding shares of Leidos common stock after consummation of the Transactions. Holders of Leidos shares prior to the transaction held the remaining 49.5% of the outstanding shares of Leidos common stock immediately after the closing.

Prior to the Distribution, Splitco incurred third-party debt financing in an aggregate principal amount of $1.8 billion and immediately thereafter, Lockheed Martin transferred the IS&GS Business to Splitco and Splitco made a special cash payment to Lockheed Martin of $1.8 billion.

In connection with the Transactions, Leidos incurred new indebtedness and assumed Splitco's indebtedness in the form of term loans in an aggregate principal amount of $690 million and $1.8 billion, respectively, and entered into a new $750 million senior secured revolving credit facility, which replaced its existing revolving credit facility. See "Note 15—Debt" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K for further information regarding the new debt incurred and the new senior revolving credit facility.

In conjunction with the Transactions, our Board of Directors declared a special dividend of $13.64 per share of Leidos common stock. Consequently, on August 22, 2016, we paid $993 million to stockholders of record as of August 15, 2016, and accrued $29 million of dividend equivalents with respect to outstanding unvested equity awards. See "Note 19—Stock-Based Compensation" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K for further information regarding the modifications made to our outstanding stock awards as a result of the special dividend.

We incurred $29 million, $77 million and $46 million of integration costs during fiscal 2018, 2017 and 2016, respectively.

After the acquisition of the IS&GS Business, we began an initiative to review our cost structure, which included optimization of our real estate portfolio by vacating facilities that were not necessary for future requirements and reducing headcount. For fiscal 2018, 2017 and 2016, we recognized $8 million, $37 million and $12 million, respectively, of restructuring expenses related to this program.

Business Environment and Trends

U.S. Government Markets

In fiscal 2018, we generated approximately 85% of our total revenues from contracts with the U.S. government, either as a prime contractor or a subcontractor to other contractors engaged in work for the U.S. government. Revenues under contracts with the DoD, including subcontracts under which the DoD is the ultimate purchaser, represented approximately 47% of our total revenues for fiscal 2018. Accordingly, our business performance is affected by the overall level of U.S. government spending, especially national security, homeland security and intelligence spending, and the alignment of our service and product offerings and capabilities with current and future budget priorities of the U.S. government.

In March 2018, Congress passed and the President signed into law the Omnibus Appropriations Bill, thereby funding the federal government through the end of the 2018 government fiscal year ("GFY"). The appropriations legislation passed earlier in the year suspended previously enacted budget caps and included a two-year budget agreement that provided $300 billion in sequestration relief for defense and non-defense spending. Defense programs saw additional funding of $80 billion and $85 billion in GFY 2018 and GFY 2019, respectively, and non-defense funding increased by $63 billion and $68 billion in GFY 2018 and GFY 2019, respectively, over the caps established in the Budget Control Act of 2011. The legislation also suspended the debt ceiling until March 2019.

In September 2018, Congress passed and the President signed a second consolidated appropriations bill funding the Departments of Defense, Labor, and Health and Human Services for the full GFY 2019. Earlier in the year, funding for the Departments of Veterans Affairs and Energy as well as funding for Congress were also enacted. All were funded at increased levels from the previous year.

The remaining seven appropriations bills were operating under a continuing resolution ("CR") until it expired on December 21, 2018. From the expiration of that CR until the passage of a new CR on January 25, 2019 there was a partial U.S. government shutdown, which reduced or delayed work on existing contracts and caused delays in other government contracting actions and payments. Prior to the expiration of the January CR, Congress passed appropriations for the seven remaining appropriations bills, thereby completing funding for GFY 2019.

Trends in the U.S. government contracting process, including a shift towards multiple-awards contracts (in which certain contractors are preapproved using indefinite-delivery/indefinite-quantity ("IDIQ") and U.S. General Services Administration ("GSA") contract vehicles) and awarding contracts on a low price, technically acceptable basis, have increased competition for U.S. government contracts, reduced backlogs by shortening periods of performance on contracts and increased pricing pressure. We expect that a majority of the business that we seek in the foreseeable future will be awarded through a competitive bidding process. For more information on these risks and uncertainties, see "Risk Factors" in Part I of this Annual Report on Form 10-K.

Table of Contents

International Markets

Sales to customers in international markets represented 9% of total revenues for fiscal 2018. Our international customers include foreign governments and their agencies, primarily located in the U.K. and Australia. Our international business increases our exposure to international markets and the associated international regulatory and geopolitical risks.

Recent changes in international trade policies, including higher tariffs on imported goods and materials, may increase our procurement costs of certain IT hardware used both on our contracts and for internal use. However, we expect to recover certain portions of these higher tariffs through our cost-plus contracts. While we are still evaluating the impact of higher tariffs, currently, we do not expect tariffs to have a significant impact to our business.

Key Performance Measures

The primary financial performance measures we use to manage our business and monitor results of operations are revenue, operating income, cash flows from operations and diluted earnings per share. Bookings and backlog are also useful measures for management and investors to evaluate our performance and potential future revenues. In addition, we consider business performance by contract type to be useful to management and investors when evaluating our operating income and margin performance.

Table of Contents
PART II

Results of Operations

Our results of operations for the periods presented were as follows:

	Year Ended			2018 to 2017		2017 to 2016	
	December 28, 2018	December 29, 2017	December 30, 2016	Dollar change	Percent change	Dollar change	Percent change
	(dollars in millions)						
Revenues	$10,194	$ 10,170	$ 7,043	$24	— %	$3,127	44 %
Cost of revenues[1]	8,690	8,738	6,103	(48)	(1)%	2,635	43 %
Selling, general and administrative expenses:							
General and administrative[1]	547	573	289	(26)	(5)%	284	98 %
Bid and proposal	136	122	89	14	11 %	33	37 %
Internal research and development	46	42	44	4	10 %	(2)	(5)%
Bad debt expense	—	10	3	(10)	(100)%	7	NM
Acquisition, integration and restructuring costs	37	139	104	(102)	(73)%	35	34 %
Asset impairment charges	7	—	4	7	100 %	(4)	(100)%
Equity earnings of non-consolidated subsidiaries	(18)	(13)	(10)	(5)	38 %	(3)	30 %
Operating income	749	559	417	190	34 %	142	34 %
Non-operating expense, net	(139)	(166)	(99)	27	(16)%	(67)	68 %
Income before income taxes	610	393	318	217	55 %	75	24 %
Income tax expense	(28)	(29)	(72)	1	(3)%	43	(60)%
Net income	582	364	246	218	60 %	118	48 %
Less: net income (loss) attributable to non-controlling interest	1	(2)	2	3	150 %	(4)	(200)%
Net income attributable to Leidos Holdings, Inc.	$581	$ 366	$ 244	$215	59 %	$122	50 %
Operating income margin	7.3 %	5.5 %	5.9 %				

NM – Not meaningful

(1) Effective the beginning of fiscal 2018, the Company established a new U.S. government Cost Accounting Standards structure and revised its disclosure statements accordingly to reflect the related cost accounting practice changes. Consequently, $185 million and $88 million was reclassified from "Cost of revenues" to "Selling, general and administrative expenses" on the consolidated statements of income for fiscal 2017 and 2016, respectively. For more information, see "Note 1—Nature of Operations and Basis of Presentation" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K.

Table of Contents
PART II

Segment and Corporate Results

Defense Solutions	Year Ended			2018 to 2017		2017 to 2016	
	December 28, 2018	December 29, 2017	December 30, 2016	Dollar change	Percent change	Dollar change	Percent change
	(dollars in millions)						
Revenues	$4,948	$ 4,959	$ 3,843	$(11)	— %	$1,116	29 %
Operating income	347	307	312	40	13 %	(5)	(2)%
Operating income margin	7.0 %	6.2 %	8.1 %				

The decrease in revenues for fiscal 2018 as compared to fiscal 2017 was primarily attributable to the completion of certain contracts and adverse impact of the foreign exchange rate movement between the U.S. dollar and Australian dollar, partially offset by new awards.
The increase in revenues for fiscal 2017 as compared to fiscal 2016 was primarily attributable to the acquired IS&GS Business of $1,146 million and growth in airborne programs, partially offset by completion of certain contracts, net volume decreases and a contract write-up in fiscal 2016.
The increase in operating income for fiscal 2018 as compared to fiscal 2017 was primarily attributable to lower amortization.
The decrease in operating income for fiscal 2017 as compared to fiscal 2016 was primarily attributable to a contract write-up in fiscal 2016 and completion of certain contracts, partially offset by the acquired IS&GS Business of $23 million.

Civil	Year Ended			2018 to 2017		2017 to 2016	
	December 28, 2018	December 29, 2017	December 30, 2016	Dollar change	Percent change	Dollar change	Percent change
	(dollars in millions)						
Revenues	$3,429	$ 3,409	$ 2,082	$20	1 %	$1,327	64 %
Operating income	290	226	146	64	28 %	80	55 %
Operating income margin	8.5 %	6.6 %	7.0 %				

The increase in revenues for fiscal 2018 as compared to fiscal 2017 was primarily attributable to new awards, favorable impact of the foreign exchange rate movement between the U.S. dollar and British pound and a net increase in program volumes, partially offset by the completion of certain contracts.
The increase in revenues for fiscal 2017 as compared to fiscal 2016 was primarily attributable to the acquired IS&GS Business of $1,528 million, partially offset by fiscal 2016 revenues from the divestiture of the heavy construction business, reduced volume on certain contracts and lower revenues from our international business, including the adverse impact of foreign exchange rates due to the movement of the exchange rate between the U.S. dollar and the British pound.
The increase in operating income for fiscal 2018 as compared to fiscal 2017 was primarily attributable to lower amortization and indirect expenditures, partially offset by net decrease in program volumes.
The increase in operating income for fiscal 2017 as compared to fiscal 2016 was primarily attributable to the acquired IS&GS Business of $78 million.

Table of Contents
PART II

Health	Year Ended			2018 to 2017		2017 to 2016	
	December 28, 2018	December 29, 2017	December 30, 2016	Dollar change	Percent change	Dollar change	Percent change
	(dollars in millions)						
Revenues	$1,817	$ 1,802	$ 1,117	$15	1 %	$685	61 %
Operating income	230	228	110	2	1 %	118	107 %
Operating income margin	12.7 %	12.7 %	9.8 %				

The increase in revenues for fiscal 2018 as compared to fiscal 2017 was primarily attributable to a net increase in program volumes and new awards, partially offset by the completion of certain contracts and lower net profit write-ups in the current year.

The increase in revenues for fiscal 2017 as compared to fiscal 2016 was primarily attributable to the acquired IS&GS Business of $685 million and growth in our federal health business, partially offset by lower volume in commercial health.

The increase in operating income for fiscal 2018 as compared to fiscal 2017 was primarily due to a net increase in program volumes, partially offset by the completion of certain contracts, higher investment costs and lower net profit write-ups in the current year.

The increase in operating income for fiscal 2017 as compared to fiscal 2016 was primarily due to the acquired IS&GS Business of $132 million, partially offset by lower volume in commercial health.

Corporate	Year Ended			2018 to 2017		2017 to 2016	
	December 28, 2018	December 29, 2017	December 30, 2016	Dollar change	Percent change	Dollar change	Percent change
	(dollars in millions)						
Revenues	$—	$ —	$ 1	$—	— %	$(1)	(100)%
Operating loss	(118)	(202)	(151)	84	(42)%	(51)	34 %

Corporate operating loss represents corporate costs that are not directly related to the operating performance of the reportable segments.

The decrease in operating loss for fiscal 2018 as compared to fiscal 2017, was primarily attributable to lower acquisition, integration and restructuring costs of $102 million, partially offset by increased legal fees and an asset impairment charge of $7 million.

The increase in operating loss for fiscal 2017 as compared to fiscal 2016, was primarily attributable to increases of $31 million of integration costs incurred related to the acquisition of the IS&GS Business and $23 million of restructuring expenses due to severance costs and lease termination expenses. This was partially offset by a decrease of $19 million of acquisition costs incurred related to the IS&GS Business. The acquisition costs incurred during fiscal 2017 were primarily attributable to a $24 million working capital adjustment recorded as a result of the settlement agreement reached.

Equity earnings of non-consolidated subsidiaries

As a result of the Transactions, we received certain non-controlling ownership interests in equity method investments. For fiscal 2018 and 2017, we recorded earnings of $28 million and $27 million, respectively, from our equity method investments, partially offset by amortization of $10 million and $14 million, respectively. For fiscal 2016, we recorded earnings of $10 million from our equity method investments.

Non-Operating Expense

Non-operating expense decreased $27 million for fiscal 2018 as compared to fiscal 2017, primarily due to a $33 million promissory note impairment that occurred during fiscal 2017, partially offset by unfavorable fair value changes on investments held in our benefit plans.

Non-operating expense increased $67 million for fiscal 2017 as compared to fiscal 2016, primarily due to interest expense associated with our term loans secured in connection with the Transactions and a $33 million promissory note impairment that occurred during fiscal 2017. The increase in non-operating expense was partially offset by favorable year-over-year foreign currency exchange movements, mostly due to the movement of the exchange rate between the U.S. dollar and the British pound.

Provision for Income Taxes

On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the “Tax Act”). The Tax Act makes broad and complex changes to the U.S. tax code, including, but not limited to, (1) reducing the U.S. federal corporate tax rate from 35% to 21%; (2) requiring companies to pay a one-time transition tax on certain unrepatriated earnings of foreign subsidiaries; (3) generally eliminating U.S. federal income taxes on dividends from foreign subsidiaries; and (4) limiting the deductibility of certain executive compensation. See “Note 20—Income Taxes” of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K for further information on the impacts of this legislation.

Our effective tax rate was 4.6%, 7.4% and 22.6% in fiscal 2018, 2017 and 2016, respectively. The effective tax rate for fiscal 2018 was favorably impacted primarily by a decrease in valuation allowances arising from the taxable conversion of a subsidiary and the utilization of capital losses, an increase in deferred tax assets related to the stock basis of a subsidiary held for sale, excess tax benefits related to employee stock-based payment transactions and federal research tax credits.

The effective tax rate for fiscal 2017 was favorably impacted primarily by the Tax Act’s reduction of the federal corporate tax rate from 35% to 21% applied to our fiscal 2017 year-end deferred tax balances and excess tax benefits related to employee stock-based payment transactions, partially offset by the impact of certain capitalized transaction costs.

The effective tax rate for fiscal 2016 was favorably impacted primarily by the tax deductibility of the special cash dividend, related to the Transactions described in “Note 6—Acquisitions” on shares held by the Leidos retirement plan, excess tax benefits related to employee stock-based payment transactions and federal research tax credits, partially offset by the impact of certain capitalized transaction costs related to the Transactions.

Non-controlling Interest

As a result of the Transactions, we received an interest in Mission Support Alliance, LLC ("MSA"), a joint venture with Centerra Group, LLC. On January 26, 2018, we entered into a Membership Interest Purchase Agreement with Jacobs Engineering Group, Inc. ("Jacobs Group"), whereby we purchased 100% of Jacobs Group's 41% outstanding membership interest in MSA. As a result, we increased our controlling ownership in MSA from 47% to 88%. We include the financial results for MSA in our consolidated financial statements. Net income attributable to non-controlling interest for fiscal 2018 and fiscal 2016 was $1 million and $2 million, respectively, compared to net loss attributable to non-controlling interest of $2 million for fiscal 2017.

Bookings and Backlog

We had net bookings of $13.7 billion and $9.7 billion during fiscal 2018 and 2017, respectively. Net bookings represent the estimated amount of revenue to be earned in the future from funded and unfunded contract awards that were received during the year, net of any adjustments to previously awarded backlog amounts. We calculate net bookings as the year’s ending backlog, plus the year’s revenues, less the prior year’s ending backlog and any impacts from foreign currency.

Backlog represents the estimated amount of future revenues to be recognized under negotiated contracts, which consists of remaining performance obligations (see "Note 4—Revenues" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K) and unexercised option periods. We segregate our backlog into two categories as follows:

- Funded Backlog. Funded backlog for contracts with the U.S. government represents the value on contracts for which funding is appropriated less revenues previously recognized on these contracts. Funded backlog for contracts with non-U.S. government entities and commercial customers represents the estimated value on contracts, which may cover multiple future years, under which we are obligated to perform, less revenues previously recognized on the contracts.
- Negotiated Unfunded Backlog. Negotiated unfunded backlog represents estimated amounts of revenue to be earned in the future from contracts for which funding has not been appropriated and unexercised priced contract options. Negotiated unfunded backlog does not include future potential task orders expected to be awarded under IDIQ, GSA Schedule or other master agreement contract vehicles, with the exception of certain IDIQ contracts where task orders are not competitively awarded and separately priced but instead are used as a funding mechanism, and where there is a basis for estimating future revenues and funding on future task orders is anticipated.

The estimated value of our total backlog for the periods presented was as follows:

	December 28, 2018	December 29, 2017
	(in millions)	
Defense Solutions:		
Funded backlog	$2,811	$ 2,384
Negotiated unfunded backlog	6,891	5,285
Total Defense Solutions backlog	$9,702	$ 7,669
Civil:		
Funded backlog	$2,314	$ 2,064
Negotiated unfunded backlog	5,079	5,321
Total Civil backlog	$7,393	$ 7,385
Health:		
Funded backlog	$1,254	$ 595
Negotiated unfunded backlog	2,483	1,827
Total Health backlog	$3,737	$ 2,422
Total:		
Funded backlog	$6,379	$ 5,043
Negotiated unfunded backlog	14,453	12,433
Total backlog	$20,832	$ 17,476

Total backlog at December 28, 2018 included an adverse impact of $171 million when compared to total backlog at December 29, 2017, due to exchange rate movements in the British pound and Australian dollar when compared to the U.S. dollar. Total backlog at December 28, 2018 included $165 million within our Civil segment attributable to our held for sale commercial cybersecurity business. See "Note 7—Divestitures" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K for more information on the expected sale.

Bookings and backlog fluctuate from period to period depending on our success rate in winning contracts and the timing of contract awards, renewals, modifications and cancellations, as well as foreign currency movements. Contract awards may be negatively impacted by ongoing industry-wide delays in procurement decisions and budget cuts by the U.S. government as discussed in “Business Environment and Trends” in this Annual Report on Form 10-K.

We expect to recognize a substantial portion of our funded backlog as revenues within the next 12 months. However, the U.S. government may cancel any contract at any time through a termination for the convenience of the U.S. government. In addition, certain contracts with commercial or non-U.S. government customers may include provisions that allow the customer to cancel at any time. Most of our contracts have cancellation terms that would permit us to recover all or a portion of our incurred costs and fees for work performed.

Contract Types

Our earnings and profitability may vary materially depending on changes in the proportionate amount of revenues derived from each type of contract. For a discussion of the types of contracts under which we generate revenues, see “Business—Contract Types” in Part I of this Annual Report on Form 10-K. Revenues by contract type as a percentage of our total revenues for the periods presented were as follows:

	Year Ended		
	December 28, 2018	December 29, 2017	December 30, 2016
Cost-reimbursement and fixed-price-incentive-fee	54 %	56 %	51 %
Firm-fixed-price	31	28	30
Time-and-materials and fixed-price-level-of-effort	15	16	19
Total	100 %	100 %	100 %

Liquidity and Capital Resources

Overview of Liquidity

As of December 28, 2018, we had $327 million in cash and cash equivalents. In addition, we have a secured revolving credit facility which can provide up to $750 million in secured borrowing capacity, if required. During fiscal 2018 and 2017, there were no borrowings outstanding under the credit facility and we were in compliance with the financial covenants.

In August 2016, our Board of Directors declared a special dividend of $13.64 per share of Leidos common stock. Consequently, on August 22, 2016, we paid $993 million to stockholders of record as of August 15, 2016, and accrued $29 million of dividend equivalents with respect to the outstanding unvested equity awards. In addition, we paid dividends of $198 million for fiscal 2018 and 2017, and $142 million for fiscal 2016.

At December 28, 2018 and December 29, 2017, we had outstanding debt of $3.1 billion. The notes outstanding as of December 28, 2018, contain financial covenants and customary restrictive covenants. We were in compliance with all covenants as of December 28, 2018.

In connection with the Transactions, Leidos incurred $2.5 billion of new indebtedness in the form of term loans (see "Note 6—Acquisitions" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K). During fiscal 2018 and 2017, we made $59 million and $209 million of principal payments, respectively, on our long-term debt, which was primarily related to our senior secured term loans. This activity included $46 million and $76 million of required quarterly payments on our term loans during fiscal 2018 and fiscal 2017, respectively. In April 2018, we made a required debt prepayment of $10 million on our senior secured term loans. The prepayment was a result of the annual excess cash flow calculation clause in our credit agreements. In addition to the required quarterly payments, we prepaid $130 million and $275 million on our term loans during fiscal 2017 and fiscal 2016, respectively (see "Note 15—Debt" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K).

During fiscal 2018, 2017 and 2016, we entered into interest rate swap agreements to hedge the cash flows on our variable rate senior secured term loans (see "Note 14—Derivative Instruments" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K). As of December 28, 2018, we had cash flow interest rate swaps on $1.5 billion of the Company's variable rate senior secured term loans. The objective of these instruments is to reduce variability in the forecasted interest payments of our variable rate secured notes.

We may from time to time seek to retire or purchase our outstanding debt through cash purchases in the open market, privately negotiated transactions or otherwise. Such repurchases, if any, will depend on prevailing market conditions, our liquidity requirements, contractual restrictions and other factors. The amounts involved may be material.

Table of Contents
PART II

Stock repurchases of Leidos common stock may be made on the open market or in privately negotiated transactions with third parties including through accelerated share repurchase ("ASR") agreements. Whether repurchases are made and the timing and actual number of shares repurchased depends on a variety of factors including price, corporate capital requirements, other market conditions and regulatory requirements. The repurchase program may be accelerated, suspended, delayed or discontinued at any time.

During fiscal 2018, we entered into an ASR agreement with a financial institution, whereby we paid an aggregate of $250 million and received approximately 4 million shares of Leidos outstanding shares of common stock during the fourth quarter of fiscal 2018 (see "Note 18—Earnings Per Share" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K). All shares delivered were immediately retired. Additionally, during fiscal 2018, we made open market repurchases of our common stock for an aggregate purchase price of $167 million. During fiscal 2017 and fiscal 2016, there were no open market repurchases of our common stock.

For the next 12 months, we anticipate that we will be able to meet our liquidity needs, including servicing our debt, through cash generated from operations, available cash balances and, if needed, borrowings from our revolving credit facility.

Summary of Cash Flows

The following table summarizes cash flow information for the periods presented:

	Year Ended December 28, 2018	December 29, 2017	December 30, 2016
	(in millions)		
Net cash provided by operating activities of continuing operations	$768	$ 526	$ 449
Net cash (used in) provided by investing activities of continuing operations	(114)	(71)	26
Net cash used in financing activities of continuing operations	(707)	(429)	(751)
Net decrease in cash, cash equivalents and restricted cash from discontinued operations	—	—	(1)
Net (decrease) increase in cash, cash equivalents and restricted cash	$(53)	$ 26	$ (277)

Net cash provided by operating activities increased $242 million for fiscal 2018 as compared to fiscal 2017. The increase was primarily due to lower payments for taxes, integration and restructuring costs and proceeds received from the termination of interest rate swaps. This was partially offset by $24 million of cash paid related to the 2016 acquisition of the IS&GS Business.

Net cash provided by operating activities increased $77 million for fiscal 2017 as compared to fiscal 2016. The increase was primarily due to the favorable timing of working capital changes, partially offset by higher integration and restructuring costs and higher payments for interest and taxes.

Net cash used in investing activities increased $43 million for fiscal 2018 as compared to fiscal 2017. The increase was primarily due to $81 million of cash paid related to the 2016 acquisition of the IS&GS Business, partially offset by $40 million of proceeds from the settlement of a promissory note.

Net cash used in investing activities increased $97 million for fiscal 2017 as compared to fiscal 2016. The increase was primarily due to cash acquired as part of the acquisition of the IS&GS Business in fiscal 2016, proceeds received from the divestiture of the heavy construction business in fiscal 2016 and higher purchases of property, plant and equipment.

Net cash used in financing activities increased $278 million for fiscal 2018 as compared to fiscal 2017. The increase was primarily due to $250 million of stock repurchases under the ASR program, $167 million of open market stock repurchases and $23 million of cash paid related to a tax indemnification liability. This was partially offset by $150 million of lower debt payments and $14 million of proceeds received from a real estate financing transaction.

Table of Contents
PART II

Net cash used in financing activities decreased $322 million for fiscal 2017 as compared to fiscal 2016. The decrease was primarily due to a special dividend cash payment in connection with the Transactions of $993 million in fiscal 2016 and decreased payments of long-term debt of $68 million, partially offset by net proceeds from debt issuance activity of $660 million in fiscal 2016 as well as higher dividend payments of $56 million and less proceeds from issuances of stock of $12 million.

Off-Balance Sheet Arrangements

We have outstanding performance guarantees and cross-indemnity agreements in connection with certain aspects of our business. We also have letters of credit outstanding principally related to performance guarantees on contracts and surety bonds outstanding principally related to performance and subcontractor payment bonds as described in "Note 26—Commitments" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K. These arrangements have not had, and management does not believe it is likely that they will in the future have, a material effect on our liquidity, capital resources, operations or financial condition.

Contractual Obligations

The following table summarizes, as of December 28, 2018, our obligations to make future payments pursuant to certain contracts or arrangements and provides an estimate of the fiscal years in which these obligations are expected to be satisfied:

	Total	2019	2020	2021	2022	2023	2024 and thereafter
	(in millions)						
Contractual obligations[1]:							
Long-term debt (including current portion)[2]	$4,318	$237	$634	$299	$212	$717	$ 2,219
Operating lease obligations	713	144	114	83	71	55	246
Capital lease obligations	3	3	—	—	—	—	—
Other long-term liabilities[3]	91	7	10	7	7	7	53
Total contractual obligations	$5,125	$391	$758	$389	$290	$779	$ 2,518

(1) We have excluded purchase orders for services or products to be delivered pursuant to U.S. government contracts for which we are entitled to full recourse under normal contract termination clauses.

(2) Includes total interest payments on our outstanding debt. Interest payments represent $161 million, $125 million, $118 million, $110 million and $98 million of the balance for fiscal 2019, 2020, 2021, 2022 and 2023, respectively, and $542 million for fiscal 2024 and thereafter. The total interest payments on our outstanding term loan debt are calculated based on the stated variable rates of the notes as of December 28, 2018. The total interest payments on our outstanding senior fixed rate secured and unsecured notes are calculated based on the stated fixed rates and do not reflect the variable interest component due to the interest rate swap agreements.

(3) Other long-term liabilities were allocated by fiscal year as follows: liabilities under deferred compensation arrangements are based upon the average annual payments in prior years upon termination of employment by participants and other liabilities are based on the fiscal year that the liabilities are expected to be realized. The table above does not include income tax liabilities for uncertain tax positions of $3 million and $4 million of other tax liabilities, as we are not able to reasonably estimate the timing of payments in individual years due to uncertainties in the timing of audit outcomes and when settlements will become due. There is no obligation included for our foreign defined benefit pension plan, as the plan is overfunded as of December 28, 2018. For a discussion of potential changes in these pension obligations, see "Note 21—Retirement Plans" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K.

Commitments and Contingencies

We are subject to a number of reviews, investigations, claims, lawsuits, other uncertainties and future obligations related to our business. For a discussion of these items, see "Note 22—Leases," "Note 25—Contingencies" and "Note 26—Commitments" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K.

Table of Contents

Critical Accounting Policies

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which are prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"). The preparation of these financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingencies at the date of the financial statements, as well as the reported amounts of revenues and expenses during the reporting periods. Management evaluates these estimates and assumptions on an ongoing basis. Our estimates and assumptions have been prepared by management on the basis of the most current and best available information. The results of these estimates form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results could differ from these estimates under different assumptions and conditions.

We have identified the following accounting policies as critical because they require significant judgments and assumptions about highly complex and inherently uncertain matters and the use of reasonably different estimates and assumptions could have a material impact on our results of operations or financial condition.

- Revenue Recognition
- Changes in Estimates on Contracts
- Goodwill Impairment
- Intangible Assets Impairment
- Income Taxes

Revenue Recognition

Our revenues from contracts with customers are from offerings including enterprise modernization; cyber operations; operations and logistics; mission software systems; integrated systems; sensors and phenomenology; and mission support, primarily with the U.S. government and its agencies. We also serve various state and local governments, foreign governments and U.S. commercial customers.

We perform under various types of contracts, which include firm-fixed-price ("FFP"), time-and-materials ("T&M"), fixed-price-level-of-effort ("FP-LOE"), cost-plus-fixed-fee, cost-plus-award-fee, cost-plus-incentive-fee and fixed-price-incentive-fee contracts.

To determine the proper revenue recognition, we first evaluate whether we have a duly approved and enforceable contract with a customer, in which the rights of the parties and payment terms are identified, and collectability is probable. We also evaluate whether two or more contracts should be combined and accounted for as a single contract, including the task orders issued under an IDIQ award. In addition, we assess contract modifications to determine whether the changes to existing contracts should be accounted for as part of the original contract or as a separate contract. Contract modifications for us generally relate to changes in contract specifications and requirements and do not add distinct services, and therefore are accounted for as part of the original contract. If contract modifications add distinct goods or services and increase the contract value by an amount that reflects the standalone selling price, those modifications are accounted for as separate contracts.

Most of our contracts are comprised of multiple promises including the design and build of software-based systems, integration of hardware and software solutions, running and maintaining of IT infrastructure and procurement services. In all cases, we assess if the multiple promises should be accounted for as separate performance obligations or combined into a single performance obligation. We generally separate multiple promises in a contract as separate performance obligations if those promises are distinct, both individually and in the context of the contract. If multiple promises in a contract are highly interrelated or require significant integration or customization within a group, they are combined and accounted for as a single performance obligation.

Our contracts with the U.S. government often contain options to renew existing contracts for an additional period of time (generally a year at a time) under the same terms and conditions as the original contract, and generally do not provide the customer any material rights under the contract. We account for renewal options as separate contracts when they include distinct goods or services at standalone selling prices.

Contracts with the U.S. government are subject to the Federal Acquisition Regulation ("FAR") and priced on estimated or actual costs of providing the goods or services. The FAR provides guidance on types of costs that are allowable in establishing prices for goods and services provided to the U.S. government and its agencies. Each contract is competitively priced and bid separately. Pricing for non-U.S. government agencies and commercial customers is based on specific negotiations with each customer. In circumstances where the standalone selling price is not directly observable, we estimate the standalone selling price using the expected cost plus margin approach. We exclude any taxes collected or imposed when determining the transaction price.

Certain of our cost-plus and fixed-price contracts contain award fees, incentive fees or other provisions that may either increase or decrease the transaction price. These variable amounts generally are awarded upon achievement of certain performance metrics, program milestones or cost targets and can be based upon customer discretion. We estimate variable consideration at the most probable amount that we expect to be entitled to, based on the assessment of the contractual variable fee criteria, complexity of work and related risks, extent of customer discretion, amount of variable consideration received historically and the potential of significant reversal of revenue.

We allocate the transaction price of a contract to our performance obligations in the proportion of its respective standalone selling prices. The standalone selling price of our performance obligations is generally based on an expected cost-plus margin approach, in accordance with the FAR. For certain product sales, we use prices from other standalone sales. Substantially all of our contracts do not contain a significant financing component, which would require an adjustment to the transaction price of the contract.

We recognize revenue on our service based contracts primarily over time as there is continuous transfer of control to the customer over the duration of the contract as we perform the promised services. For U.S. government contracts, continuous transfer of control to the customer is evidenced by clauses in the contract that allow the customer to unilaterally terminate the contract for convenience, pay for costs incurred plus a reasonable profit and take control of any work-in-process. Similarly, for non-U.S. government contracts, the customer typically controls the work-in-process as evidenced by rights to payment for work performed to date plus a reasonable profit to deliver products or services that do not have an alternate use to us. Anticipated losses on service based contracts are recognized when known. In certain product sales, where the products have an alternate use, we recognize revenue at a point in time when the customer takes control of the asset usually denoted by possession and legal title.

On FFP contracts, revenue recognized over time generally uses a method that measures the extent of progress towards completion of a performance obligation, principally using a cost-input method (referred to as the cost-to-cost method). Under the cost-to-cost method, revenue is recognized based on the proportion of total costs incurred to estimated total costs-at-completion ("EAC"). A performance obligation's EAC includes all direct costs such as materials, labor, subcontract costs, overhead and a ratable portion of general and administrative costs. In addition, we include in an EAC of a performance obligation future losses estimated to be incurred on onerous contracts, as and when known. On certain other contracts, principally T&M, FP-LOE, and cost-plus, revenue is recognized using the right-to-invoice practical expedient as we are contractually able to invoice the customer based on the control transferred to the customer. Additionally, on maintenance (generally FFP) performance obligations, revenue is recognized over time using a straight-line method as the control of the services is provided to the customer evenly over the period of performance.

For certain performance obligations, we are not primarily responsible for fulfilling the promise to provide the goods or service to the customer, do not have inventory risk and do not have discretion in establishing the price for the goods or service. In such cases, we recognize revenue on a net basis.

Changes in Estimates on Contracts

Changes in estimates related to contracts accounted for using the cost-to-cost method of accounting are recognized in the period in which such changes are made for the inception-to-date effect of the changes, with the exception of contracts acquired through the acquisition of the IS&GS Business, where the adjustment is made for the period commencing from the date of acquisition.

Changes in estimates on contracts for the periods presented were as follows:

	Year Ended December 28, 2018	December 29, 2017	December 30, 2016
	(in millions, except for per share amounts)		
Net favorable impact to income before income taxes	$105	$ 103	$ 37
Impact on diluted EPS attributable to Leidos common stockholders	$0.52	$ 0.41	$ 0.22

The increase in the changes in estimates on contracts from fiscal 2016 to fiscal 2017 is primarily due to completion of contracts or events which mitigated risk and due to the finalization of award and incentive fees.

The impact on diluted EPS attributable to Leidos common stockholders is calculated using our statutory tax rate.

During fiscal 2018, revenue recognized from performance obligations satisfied in previous periods was $102 million. The changes primarily relate to revisions of variable consideration, including award fees, and revisions to estimates at completion resulting from changes in contract scope, mitigation of contract risks or due to true-ups of contract estimates at the end of contract performance.

Goodwill Impairment

Goodwill represents the excess of the fair value of consideration transferred, plus the fair value of any non-controlling interests in the acquiree, over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. Goodwill is not amortized, but instead is tested annually for impairment at the reporting unit level and tested more frequently if events or circumstances indicate that the carrying value may not be recoverable. Our policy is to perform our annual goodwill impairment evaluation as of the first day of the fourth quarter of our fiscal year. During fiscal 2018, we had five reporting units for the purpose of testing goodwill for impairment.

Goodwill is evaluated for impairment either under a qualitative assessment option or a quantitative approach depending on the facts and circumstances of a reporting unit, consideration of the excess of a reporting unit's fair value over its carrying amount in previous assessments and changes in business environment.

When performing a qualitative assessment, we consider factors including, but not limited to, current macroeconomic conditions, industry and market conditions, cost factors, financial performance and other events relevant to the entity or reporting unit under evaluation to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If we determine that it is more likely than not that a reporting unit’s fair value is less than its carrying amount, a quantitative goodwill impairment test is performed.

When performing a quantitative goodwill impairment test, the reporting unit carrying value is compared to its fair value. Goodwill is deemed impaired if, and the impairment loss is recognized for the amount by which, the reporting unit carrying value exceeds its fair value. For fiscal 2018, a qualitative analysis was performed for four of our reporting units and a quantitative step one analysis was performed for one reporting unit. A quantitative analysis was performed for all reporting units for fiscal 2017.

We estimate the fair value of each reporting unit using both market and income approaches when a quantitative analysis is performed. To determine the fair value of the reporting units, the outputs from both methods are equally weighted.

The market approach is a technique where the fair value is calculated based on the multiples of comparable publicly-traded companies that provide a reasonable basis of comparison with each of our reporting units. Valuation ratios are selected that relate market prices to selected financial metrics from comparable companies. These ratios are applied after consideration of adjustments and weightings related to financial position, growth, volatility, working capital movement and other factors. Due to the fact that stock prices of comparable companies represent minority interests, we also consider an acquisition control premium to reflect the impact of additional value associated with a controlling interest.

The income approach is a technique where the fair value is calculated based on present value future cash flows using risk-adjusted discount rates, which represent the weighted-average cost of capital ("WACC") for each reporting unit. Determination of WACC includes assessing the cost of equity and debt as of the valuation date. In addition, a terminal value is developed for forecasted future cash flows beyond the projection period discounted back to the present value. The forecasts used in our estimation of fair value are developed by management based on business and market considerations.

The goodwill impairment test process and valuation model is based upon certain key assumptions that require the exercise of significant judgment and assumptions including the use of appropriate financial projections, economic expectations, WACC and expected long-term growth rates, as well as using available market data. Significant changes to these estimates and assumptions could adversely impact our conclusions and actual future results may differ from the estimates. In addition, the identification of reporting units and the allocation of assets and liabilities to the reporting units when determining the carrying value of each reporting unit also requires judgment.

Based on a qualitative analysis performed during our annual impairment evaluation for fiscal 2018 for certain of our reporting units, it was determined that it is more likely than not that the fair values of the reporting units were in excess of the individual reporting unit carrying values, and as a result, a quantitative step one analysis was not necessary. Additionally, based on the results of the quantitative step one analysis for one of our reporting units, it was determined that the fair value significantly exceeded the reporting unit's carrying value. We did not recognize any goodwill impairments during 2018, 2017 or 2016.

By definition, assumptions used in estimating the fair value of a reporting unit are judgmental and inherently uncertain. A significant change in the economic conditions of a reporting unit, such as declines in business performance, changes in government fiscal policies, deterioration in market conditions, adverse estimates of regulatory or legislative changes or increases in the estimated cost of equity, could cause the estimated fair values of our reporting units to decline in the future and increase the risk of a goodwill impairment charge to earnings in a future period.

Intangible Assets Impairment

Intangible assets with finite lives are assessed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Intangible assets with indefinite lives are not amortized but are assessed for impairment at the beginning of the fourth quarter and whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Additionally, indefinite-lived intangible assets are not being amortized until such time that the useful life is determined to no longer be indefinite.

There were no intangible asset impairment charges recognized in fiscal 2018, 2017 and 2016. The net carrying value of intangible assets as of December 28, 2018, was $652 million.

Income Taxes

We account for income taxes under the asset and liability method of accounting, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities. Under this method, changes in tax rates and laws are recognized in income in the period such changes are enacted. The provision for federal, state, foreign and local income taxes is calculated on income before income taxes based on current tax law and includes the cumulative effect of any changes in tax rates from those used previously in determining deferred tax assets and liabilities. Such provision differs from the amounts currently payable because certain items of income and expense are recognized in different reporting periods for financial reporting purposes than for income tax purposes.

Recording our provision for income taxes requires management to make significant judgments and estimates for matters whose ultimate resolution may not become known until the final resolution of an examination by the IRS or state agencies. Additionally, recording liabilities for uncertain tax positions involves significant judgment in evaluating our tax positions and developing our best estimate of the taxes ultimately expected to be paid.

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

We also recognize liabilities for uncertain tax positions when it is more likely than not that a tax position will not be sustained upon examination and settlement with various taxing authorities. Liabilities for uncertain tax positions are measured based upon the largest amount of benefit that is greater than 50% likely to be realized upon ultimate settlement. We have experienced years when liabilities for uncertain tax positions were settled for amounts different from recorded amounts as described in "Note 20—Income Taxes" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K.

Recently Adopted and Issued Accounting Pronouncements

For a discussion of these items, see "Note 2—Accounting Standards" of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to certain market risks in the normal course of business. Our current market risk exposures are primarily related to interest rates and foreign currency fluctuations. The following information about our market sensitive financial instruments contains forward-looking statements.

Interest Rate Risk

Our exposure to market risk for changes in interest rates relates primarily to long-term debt obligations and derivatives. Our policy authorizes, with Board of Directors' approval, the limited use of derivative instruments to hedge specific interest rate risks.

Debt and derivatives

At December 28, 2018 and December 29, 2017, we had $3.1 billion of fixed and variable rate debt. During fiscal 2016, in connection with the acquisition of the IS&GS Business, Leidos, Inc. secured a new term loan of $690 million. As a result of the acquisition, Leidos assumed the IS&GS Business' term loans of $1.8 billion, which were obtained by the IS&GS Business immediately prior to the Transactions. These senior secured term loans have variable stated interest rates that are determined based on the LIBOR rate plus a margin. As a result, we may experience fluctuations in interest expense.

We have interest rate swap agreements to hedge the cash flows of a portion of our variable rate senior secured term loans ("Variable Rate Loans"). Under the terms of the interest rate swap agreements, we receive variable interest payments based on the one-month LIBOR rate and pay interest at a fixed rate. The interest rate swap agreements on $1.1 billion of our Variable Rate Loans had a maturity date of December 2021 and a fixed interest rate of 1.08%. The interest rate swap agreements on $300 million and $250 million of our Variable Rate Loans had a maturity date of August 2022 and fixed interest rates of 1.66% and 2.59%, respectively. During fiscal 2018, we terminated these interest rate swaps and entered into new interest rate swap agreements, which mature in August 2025 and have a fixed interest rate of 3.00%, to hedge the cash flows of $1.5 billion of our Variable Rate Loans. The interest rate swap agreements effectively converted a portion of our variable rate borrowings to fixed rate borrowings. As of December 28, 2018, and December 29, 2017, the fair value of our interest rate swap agreements with respect to our variable rate senior secured loans was a $32 million liability and a $37 million asset, respectively.

Additionally, we have interest rate swap agreements with respect to all of the $450 million aggregate principal outstanding on our fixed rate 4.45% notes maturing in December 2020. The interest rate swap agreements effectively converted a portion of our fixed-rate debt to floating-rate debt tied to the changes in the six-month LIBOR benchmark interest rate. As a result, we may experience fluctuations in interest expense. Under the terms of the interest rate swap agreements, we will receive semi-annual interest payments at the coupon rate of 4.45% and will pay variable interest based on the six-month LIBOR rate. As of December 28, 2018, and December 29, 2017, the fair value of our interest rate swaps with respect to our fixed rate debt was a $3 million liability and an immaterial amount, respectively.

Table of Contents

The counterparties to these agreements are financial institutions. We do not hold or issue derivative financial instruments for trading or speculative purposes. We cannot predict future market fluctuations in interest rates and their impact on our interest rate swaps. For fiscal 2018 and fiscal 2017, a hypothetical 10% movement in the six-month LIBOR rate would result in a $15 million and $8 million amount, respectively, related to our annual interest expense due to the interest rate swaps. For fiscal 2018 and fiscal 2017, a hypothetical 10% movement in the one-month LIBOR rate would result in a $12 million and $11 million amount, respectively, related to our annual interest expense due to the interest rate swaps and variable rate debt. The net hypothetical 10% movement in the six-month and one-month LIBOR rates would not have a significant impact on our annual interest expense. For additional information related to our interest rate swap agreements and debt, see "Note 14—Derivative Instruments" and "Note 15—Debt," respectively, of the notes to the consolidated financial statements contained within this Annual Report on Form 10-K.

Cash and Cash Equivalents

As of December 28, 2018, and December 29, 2017, our cash and cash equivalents included investments in several large institutional money market funds and bank deposits. For fiscal 2018 and fiscal 2017, a hypothetical 10% interest rate movement would not have a significant impact on the value of our holdings or on interest income.

Foreign Currency Risk

Although the majority of our transactions are denominated in U.S. dollars, some of our transactions are denominated in foreign currencies. Our foreign currency exchange rate risk relates to receipts from customers, payments to suppliers and certain intercompany transactions denominated in currencies other than our (or one of our subsidiaries') functional currency. Our foreign operations represented 9% of total revenues for both fiscal 2018 and fiscal 2017.

Item 8. Financial Statements and Supplementary Data

LEIDOS HOLDINGS, INC.
INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

Financial statement schedules are omitted because they are not applicable or the required information is presented in the consolidated financial statements or the notes thereto.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the shareholders and the Board of Directors of Leidos Holdings, Inc.
Reston, Virginia

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Leidos Holdings, Inc. and subsidiaries (the "Company") as of December 28, 2018 and December 29, 2017, the related consolidated statements of income, comprehensive income, equity, and cash flows, for the fiscal years ended December 28, 2018, December 29, 2017, and December 30, 2016 and the related notes (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 28, 2018, December 29, 2017, and the results of its operations and its cash flows for the fiscal years ended December 28, 2018, December 29, 2017, and December 30, 2016, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of December 28, 2018, based on criteria established in Internal Control — Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 19, 2019, expressed an unqualified opinion on the Company's internal control over financial reporting.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Deloitte & Touche LLP
McLean, Virginia
February 19, 2019
We have served as the Company's auditor since fiscal 2000.

Table of Contents

LEIDOS HOLDINGS, INC.
CONSOLIDATED BALANCE SHEETS

	December 28, 2018	December 29, 2017
	(in millions)	
ASSETS		
Cash and cash equivalents	$327	$ 390
Receivables, net	1,877	1,831
Other current assets	543	453
Assets held for sale	92	—
Total current assets	2,839	2,674
Property, plant and equipment, net	237	232
Intangible assets, net	652	856
Goodwill	4,860	4,974
Other assets	182	254
	$8,770	$ 8,990
LIABILITIES AND EQUITY		
Accounts payable and accrued liabilities	$1,476	$ 1,639
Accrued payroll and employee benefits	473	487
Dividends payable	12	17
Income taxes payable	3	4
Long-term debt, current portion	72	55
Liabilities held for sale	23	—
Total current liabilities	2,059	2,202
Long-term debt, net of current portion	3,052	3,056
Deferred tax liabilities	170	220
Other long-term liabilities	178	129
Commitments and contingencies (Notes 22, 25 and 26)		
Stockholders' equity:		
Preferred stock, $.0001 par value,10 million shares authorized and no shares issued and outstanding at December 28, 2018, and December 29, 2017	—	—
Common stock, $.0001 par value, 500 million shares authorized, 146 million and 151 million shares issued and outstanding at December 28, 2018, and December 29, 2017, respectively	—	—
Additional paid-in capital	2,966	3,344
Accumulated earnings (deficit)	372	(7)
Accumulated other comprehensive (loss) income	(30)	33
Total Leidos stockholders' equity	3,308	3,370
Non-controlling interest	3	13
Total equity	3,311	3,383
	$8,770	$ 8,990

See accompanying notes to consolidated financial statements.

Table of Contents

LEIDOS HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF INCOME

	Year Ended		
	December 28, 2018	December 29, 2017	December 30, 2016
	(in millions, except per share amounts)		
Revenues	$10,194	$ 10,170	$ 7,043
Cost of revenues	8,690	8,738	6,103
Selling, general and administrative expenses	729	737	422
Bad debt expense	—	10	3
Acquisition, integration and restructuring costs	37	139	104
Asset impairment charges	7	—	4
Equity earnings of non-consolidated subsidiaries	(18)	(13)	(10)
Operating income	749	559	417
Non-operating expense:			
Interest expense, net	(138)	(140)	(86)
Other expense, net	(1)	(26)	(13)
Income before income taxes	610	393	318
Income tax expense	(28)	(29)	(72)
Net income	582	364	246
Less: net income (loss) attributable to non-controlling interest	1	(2)	2
Net income attributable to Leidos common stockholders	$581	$ 366	$ 244
Earnings per share:			
Basic	$3.85	$ 2.41	$ 2.39
Diluted	3.80	2.38	2.35

See accompanying notes to consolidated financial statements.

Table of Contents

LEIDOS HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Year Ended		
	December 28, 2018	December 29, 2017	December 30, 2016
	(in millions)		
Net income	$582	$ 364	$ 246
Foreign currency translation adjustments	(61)	24	(7)
Unrecognized (loss) gain on derivative instruments	(10)	4	14
Pension adjustments	(1)	9	(3)
Total other comprehensive (loss) income, net of taxes	(72)	37	4
Comprehensive income	510	401	250
Less: comprehensive income (loss) attributable to non-controlling interest	1	(2)	2
Comprehensive income attributable to Leidos common stockholders	$509	$ 403	$ 248

See accompanying notes to consolidated financial statements.

Table of Contents

LEIDOS HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF EQUITY

	Shares of common stock	Additional paid-in capital	Accumulated earnings (deficit)	Accumulated other comprehensive (loss) income	Leidos Holdings, Inc. stockholders' equity	Non-controlling interest	Total
	(in millions, except for per share amounts)						
Balance at January 1, 2016	72	$ 1,353	$ (277)	$ (8)	$ 1,068	$ —	$ 1,068
Net income	—	—	244	—	244	2	246
Other comprehensive income, net of taxes	—	—	—	4	4	—	4
Issuances of stock (less forfeitures)	1	36	—	—	36	—	36
Repurchases of stock and other	—	(24)	—	—	(24)	—	(24)
Dividends of $1.28 per share	—	—	(144)	—	(144)	—	(144)
Special cash dividend of $13.64 per share	—	(1,022)	—	—	(1,022)	—	(1,022)
Stock-based compensation	—	35	—	—	35	—	35
Stock issued for the IS&GS Business acquisition	77	2,938	—	—	2,938	—	2,938
Equity interest acquired	—	—	—	—	—	10	10
Balance at December 30, 2016	150	3,316	(177)	(4)	3,135	12	3,147
Net income (loss)	—	—	366	—	366	(2)	364
Other comprehensive income, net of taxes	—	—	—	37	37	—	37
Issuances of stock (less forfeitures)	1	16	—	—	16	—	16
Repurchases of stock and other	—	(31)	—	—	(31)	—	(31)
Dividends of $1.28 per share	—	—	(196)	—	(196)	—	(196)
Stock-based compensation	—	43	—	—	43	—	43
Adjustment to original purchase price allocation	—	—	—	—	—	3	3
Balance at December 29, 2017	151	3,344	(7)	33	3,370	13	3,383
Cumulative adjustments related to ASU adoptions	—	—	(8)	9	1	—	1
Balance at December 30, 2017	151	3,344	(15)	42	3,371	13	3,384
Net income	—	—	581	—	581	1	582
Other comprehensive loss, net of taxes	—	—	—	(72)	(72)	—	(72)
Issuances of stock (less forfeitures)	1	17	—	—	17	—	17
Repurchases of stock and other	(6)	(438)	—	—	(438)	—	(438)
Dividends of $1.28 per share	—	—	(194)	—	(194)	—	(194)
Stock-based compensation	—	44	—	—	44	—	44
Purchase of a non-controlling interest	—	(1)	—	—	(1)	(10)	(11)
Other	—	—	—	—	—	(1)	(1)
Balance at December 28, 2018	146	$ 2,966	$ 372	$ (30)	$ 3,308	$ 3	$ 3,311

See accompanying notes to consolidated financial statements.

Table of Contents

LEIDOS HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 28, 2018	December 29, 2017	December 30, 2016
	(in millions)		
Cash flows from operations:			
Net income	$582	$ 364	$ 246
Adjustments to reconcile net income to net cash provided by continuing operations:			
Depreciation and amortization	257	336	122
Amortization of equity method investments	10	14	—
Stock-based compensation	44	43	35
Asset impairment charges	7	—	4
Non-cash interest expense	6	12	4
Promissory note impairment	—	33	—
Bad debt expense	—	10	3
Other	2	9	(7)
Change in assets and liabilities, net of effects of acquisitions and dispositions:			
Receivables	(58)	(191)	123
Other current assets	(73)	(76)	(98)
Accounts payable and accrued liabilities	(46)	152	(25)
Accrued payroll and employee benefits	(12)	8	26
Deferred income taxes and income taxes receivable/payable	(39)	(151)	36
Other long-term assets/liabilities	88	(37)	(20)
Net cash provided by operating activities of continuing operations	768	526	449
Cash flows from investing activities:			
Payments for property, plant and equipment	(73)	(81)	(29)
Collections on promissory note	40	2	4
Acquisitions of businesses	(81)	—	25
Net proceeds from sale of assets	—	8	3
Proceeds from disposition of business	—	—	23
Net cash (used in) provided by investing activities of continuing operations	(114)	(71)	26

Table of Contents
LEIDOS HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS [CONTINUED]

	Year Ended December 28, 2018	December 29, 2017	December 30, 2016
	(in millions)		
Cash flows from financing activities:			
Payments of long-term debt	(59)	(209)	(277)
Proceeds from debt issuance	—	—	690
Payments for debt issuance and modification costs	(8)	(4)	(30)
Proceeds from issuances of stock	14	13	25
Repurchases of stock and other	(438)	(31)	(24)
Special cash dividend payment	—	—	(993)
Dividend payments	(198)	(198)	(142)
Payment of tax indemnification liability	(23)	—	—
Proceeds from real estate financing transaction	14	—	—
Payments for non-controlling interest acquired	(8)	—	—
Other	(1)	—	—
Net cash used in financing activities of continuing operations	(707)	(429)	(751)
Net (decrease) increase in cash, cash equivalents and restricted cash from continuing operations	(53)	26	(276)
Cash flows from discontinued operations:			
Net cash used in investing activities of discontinued operations	—	—	(1)
Net decrease in cash, cash equivalents and restricted cash from discontinued operations	—	—	(1)
Net (decrease) increase in cash, cash equivalents and restricted cash	(53)	26	(277)
Cash, cash equivalents and restricted cash at beginning of year	422	396	673
Cash, cash equivalents and restricted cash at end of year	$369	$ 422	$ 396

See accompanying notes to consolidated financial statements.

LEIDOS HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
Note 1—Nature of Operations and Basis of Presentation
Nature of Operations and Basis of Presentation

Leidos Holdings, Inc. ("Leidos"), a Delaware corporation, is a holding company whose direct 100%-owned subsidiary and principal operating company is Leidos, Inc. Leidos is a FORTUNE 500® science, engineering and information technology company that provides services and solutions in the defense, intelligence, civil and health markets. Leidos' domestic customers include the U.S. Department of Defense ("DoD"), the U.S. Intelligence Community, the U.S. Department of Homeland Security ("DHS"), the Federal Aviation Administration, the Department of Veterans Affairs and many other U.S. government civilian agencies, as well as state and local government agencies. Leidos' international customers include foreign governments and their agencies, primarily located in Australia and the United Kingdom ("U.K."). Unless indicated otherwise, references to the "Company," "we," "us" and "our" refer collectively to Leidos Holdings, Inc. and its consolidated subsidiaries.

On August 16, 2016, a wholly-owned subsidiary of Leidos Holdings, Inc. merged with the Information Systems & Global Solutions business (the "IS&GS Business") of Lockheed Martin Corporation in a Reverse Morris Trust transaction (see "Note 6—Acquisitions" for further information). The acquired IS&GS Business was renamed Leidos Innovations Corporation. On December 28, 2018, Leidos Innovations Corporation was merged into Leidos, Inc. As a result of the Lockheed Martin transaction, the Company received a controlling interest in Mission Support Alliance, LLC ("MSA"), a joint venture with Centerra Group, LLC and Jacobs Engineering Group, Inc. ("Jacobs Group"). On January 26, 2018, the Company entered into a Membership Interest Purchase Agreement with Jacobs Group, whereby the Company purchased 100% of Jacobs Group's 41% outstanding membership interest in MSA. As a result, Leidos increased its controlling ownership in MSA from 47% to 88%. The Company consolidates the financial results for MSA into its consolidated financial statements.

The consolidated financial statements also include the balances of all voting interest entities in which Leidos has a controlling voting interest ("subsidiaries") and a variable interest entity ("VIE") in which Leidos is the primary beneficiary. The consolidated balances of the Company's VIE are not material to the Company's consolidated financial statements for the periods presented. Intercompany accounts and transactions between consolidated companies have been eliminated in consolidation.

During fiscal 2017, the Company completed its business reorganization, which resulted in identification of three reportable segments (Defense Solutions, Civil and Health). Additionally, the Company separately presents the costs associated with corporate functions as Corporate. The Company commenced operating and reporting under the new organizational structure effective the beginning of fiscal 2017. As a result of this change, fiscal 2016 segment results and disclosures have been recast to reflect the new reportable segments (see "Note 24—Business Segments").

Certain amounts in the prior year financial statements have been reclassified to conform to the current year presentation. The Company classifies indirect costs incurred within or allocated to its U.S. government customers as overhead (included in "Cost of revenues") or general administrative expenses in the same manner as such costs are defined in the Company's disclosure statements under U.S. government Cost Accounting Standards ("CAS"). Effective the beginning of fiscal 2018, the Company established a new CAS structure and revised its disclosure statements accordingly to reflect the related cost accounting practice changes. Consequently, $185 million and $88 million was reclassified from "Cost of revenues" to "Selling, general and administrative expenses" on the consolidated statements of income for fiscal 2017 and 2016, respectively.

The Company aggregated "Acquisition and integration costs" and "Restructuring expenses" into "Acquisition, integration and restructuring costs", and "Interest income" and "Interest expense" into "Interest expense, net" on the consolidated statements of income. Additionally, the Company separately disclosed "Collections on promissory note", which was previously included in "Other" within investing cash flows on the consolidated statements of cash flows.

Note 2—Accounting Standards

Accounting Standards Updates Adopted

During fiscal 2018, the Company adopted the following Accounting Standards Updates ("ASU"):

ASU 2014-09, Revenue from Contracts with Customers (Topic 606)

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update 2014-09 ("ASC 606") and related amendments, which superseded all prior revenue recognition methods and industry-specific guidance. The core principle of ASC 606 is an entity should recognize revenue to depict the transfer of control for promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In applying the revenue principles, an entity is required to identify the contract(s) with a customer, identify the performance obligations, determine the transaction price, allocate the transaction price to the performance obligations and recognize revenue when the performance obligation is satisfied (i.e., either over time or point in time). ASC 606 further requires that companies disclose sufficient information to enable users of financial statements to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers.

ASC 606 provided companies an option of two transition methods, the full retrospective method, in which case the standard would be applied to each prior reporting period presented and the cumulative effect of applying the standard would be recognized at the earliest period shown, or the modified retrospective method, in which case the cumulative effect of applying the standard would be recognized at the date of initial application. The ASU was effective for annual reporting periods beginning after December 15, 2017.

Effective December 30, 2017 (the beginning of fiscal 2018), the Company adopted the requirements of ASC 606 using the modified retrospective method. The guidance was not applied to contracts that were complete at December 30, 2017, and the comparative information for the prior fiscal years have not been retrospectively adjusted.

As a result of the adoption the Company recorded a $1 million decrease to its beginning accumulated deficit as the cumulative impact of adoption of the new revenue standard. The primary impact was on certain units-of-delivery contracts, as the Company previously recognized revenue at a point in time when the customer accepted delivery of the product or service. Under ASC 606, revenues on certain units-of-delivery contracts are now recognized using an over-time model. The adoption of ASC 606 did not have a significant impact on the Company's revenue recognition policy as revenues on substantially all of the Company's contracts continue to be recognized over time.

In adopting ASC 606, the Company elected to use certain practical expedients permitted by the standard including using the portfolio approach where contracts with similar characteristics were assessed collectively to evaluate risk over the impact of ASC 606. The Company also elected to adopt the right-to-invoice practical expedient on certain cost-reimbursable contracts where the Company recognizes revenues as it is contractually able to invoice the customer based on the control transferred to the customer.

ASU 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedge Activities

In August 2017, the FASB issued ASU 2017-12, which simplifies the application of hedge accounting and improves the financial reporting of hedging relationships to better portray the economic results of an entity's risk management activities. The ASU is effective for public companies for annual reporting periods beginning after December 15, 2018, and should be applied on a modified retrospective basis. Early adoption is permitted.

The Company early adopted the provisions of ASU 2017-12 using the modified retrospective method during the first quarter of fiscal 2018, and recorded a $3 million increase to accumulated other comprehensive income and a corresponding increase to beginning accumulated deficit for the cumulative ineffectiveness gains related to the cash flow hedges.

ASU 2018-02, Income Statement–Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income

In February 2018, the FASB issued ASU 2018-02, which allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act ("Tax Act"). This ASU is effective for all entities for annual reporting periods beginning after December 15, 2018, and should be applied either in the period of adoption or retrospectively to each period in which the effect of the change in the U.S. federal corporate income tax rate due to the Tax Act is recognized. Early adoption is permitted.

The Company early adopted the provisions of ASU 2018-02 during the first quarter of fiscal 2018 (applied in the period of adoption), and recorded a $6 million increase to accumulated other comprehensive income and a corresponding increase to beginning accumulated deficit to reflect the changes in the U.S. federal corporate income tax rate as a result of the Tax Act. As a result of the adoption of ASU 2018-02, the Company's policy to release income tax effects in accumulated other comprehensive income is consistent with the underlying book method.

The cumulative effect of the changes made to the Company's consolidated balance sheet for the adoptions of the ASUs above was as follows:

	Balance at December 29, 2017	Adjustments due to ASU 2014-09	Adjustments due to ASU 2017-12	Adjustments due to ASU 2018-02	Balance at December 30, 2017
	(in millions)				
Assets:					
Receivables, net	$1,831	$ 4	$ —	$ —	$ 1,835
Other current assets	453	(3)	—	—	450
Equity:					
Accumulated deficit	$(7)	$ 1	$ (3)	$ (6)	$ (15)
Accumulated other comprehensive income	33	—	3	6	42

Accounting Standards Updates Issued But Not Yet Adopted

ASU 2016-02, ASU 2018-10, ASU 2018-11 and ASU 2018-20, Leases (Topic 842)

In February 2016, the FASB issued ASU 2016-02, which supersedes the current lease guidance under Leases (Topic 840) and makes several changes, such as requiring an entity to recognize a right-of-use ("ROU") asset and corresponding lease obligation on the balance sheet, classified as financing or operating, as appropriate. The update is effective for public companies for annual and interim reporting periods beginning after December 15, 2018, and should be adopted under the modified retrospective approach.

In July 2018, the FASB issued ASU 2018-10 "Codification Improvements to Topic 842, Leases" to add clarity to certain areas within ASU 2016-02 and ASU 2018-11 "Targeted Improvements", to add an additional and optional transition method to adopt the new leases standard by allowing recognition of a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. In December 2018, the FASB issued ASU 2018-20 "Narrow-Scope Improvements for Lessors" to add clarity to lessors accounting for sales taxes and other similar taxes collected from lessees, accounting for variable payments for contracts with lease and non-lease components, and accounting for certain lessor costs. The effective date and transition requirements of these updates will be the same as ASU 2016-02.

The Company plans to adopt the new lease accounting standards in fiscal 2019 using the optional transition method. The Company has made progress in reviewing lease and other service based contracts, implementing a new lease accounting and administration software solution, establishing new processes and internal controls. The Company has elected to adopt certain practical expedients provided under ASC 842, including the option to not apply lease recognition for short-term leases, reassessment of whether expired or existing contracts contain leases, reassessment of lease classification for expired or existing leases, applying a single discount rate to a portfolio of leased assets with similar durations, reassessing initial direct costs and combining lease and non-lease components in revenue arrangements.

The Company expects the adoption of the new standard will result in the recognition of at least $350 million and $400 million of ROU assets and lease liabilities, respectively, primarily due to its operating leases, to the Company's consolidated balance sheets, but will not have a material impact on the consolidated statements of income and consolidated statements of cash flows. The Company's accounting for capital leases will remain substantially unchanged. Additionally, the Company estimates a $65 million increase in retained earnings due to the cumulative effect of recognizing a gain related to the sale and leaseback of the San Diego properties (see "Note 22—Leases").

ASU 2016-13, Financial Instruments – Credit Losses (Topic 326)

In June 2016, the FASB issued ASU 2016-13, which eliminates the requirement that a credit loss on a financial instrument be "probable" prior to recognition. Instead, a valuation allowance will be recorded to reflect an entity's current estimate of all expected credit losses, based on both historical and forecasted information related to an instrument. The update is effective for public companies for annual and interim reporting periods beginning after December 15, 2019, and should be adopted using a modified retrospective approach, which applies a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective. A prospective approach is required for debt securities for which an other-than-temporary impairment had been recognized before the effective date and loans and debt securities acquired with deteriorated credit quality. Early adoption is permitted. The Company is evaluating the provisions of ASU 2016-13 and its impact on the Company's consolidated financial position, results of operations and cash flows.

ASU 2018-15, Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement (Subtopic 350-40)

In August 2018, the FASB issued ASU 2018-15, which aligns the capitalization requirements for implementation costs incurred in a hosting arrangement that is a service contract with the existing capitalization requirements for implementation costs associated with internal-use software. The update is effective for public companies for annual and interim reporting periods beginning after December 15, 2019, and may be adopted either retrospectively or prospectively. Early adoption is permitted. The Company is evaluating the provisions of ASU 2018-15 and its impact on the Company’s consolidated financial position, results of operations and cash flows.

Note 3—Summary of Significant Accounting Policies

Reporting Periods

Leidos' fiscal year ends on the Friday nearest the end of December. Fiscal 2018, 2017 and 2016 each included 52 weeks.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingencies at the date of the financial statements, as well as the reported amounts of revenues and expenses during the reporting periods. Management evaluates these estimates and assumptions on an ongoing basis, including those relating to estimated profitability of long-term contracts, indirect billing rates, allowances for doubtful accounts, inventories, fair value and impairment of intangible assets and goodwill, income taxes, pension benefits, stock-based compensation expense and contingencies. These estimates have been prepared by management on the basis of the most current and best available information; however, actual results could differ materially from those estimates.

Operating Cycle

The Company's operating cycle for long-term contracts may be greater than one year and is measured by the average time intervening between the inception and the completion of those contracts.

Business Combinations, Investments and Variable Interest Entities

Business Combinations

The accounting for business combinations requires the Company to make judgments and estimates related to the fair value of assets acquired, including the identification and valuation of intangible assets, as well as liabilities and contingencies assumed. Such judgments and estimates directly impact the amount of goodwill recognized in connection with an acquisition.

Investments

Investments in entities and corporate joint ventures where the Company has a non-controlling ownership interest but over which the Company has the ability to exercise significant influence, are accounted for under the equity method of accounting whereby the Company recognizes its proportionate share of the entities' net income or loss and does not consolidate the entities' assets and liabilities.

Equity investments in entities over which the Company does not have the ability to exercise significant influence and whose securities do not have a readily determinable fair value are carried at cost or cost net of other-than-temporary impairments.

Variable Interest Entities

The Company occasionally forms joint ventures and/or enters into arrangements with special purpose limited liability companies for the purpose of bidding and executing on specific projects. The Company analyzes each such arrangement to determine whether it represents a VIE. If the arrangement is determined to be a VIE, the Company assesses whether it is the primary beneficiary of the VIE and is consequently required to consolidate the VIE.

Divestitures

From time-to-time, the Company may dispose (or management may commit to plans to dispose) of strategic or non-strategic components of the business. Divestitures representing a strategic shift in operations are classified as discontinued operations for all periods presented. Non-strategic divestitures are not reclassified as discontinued operations and remain in continuing operations.

Restructuring Expenses

Restructuring expenses are incurred in connection with programs aimed at reducing the Company's costs and primarily include lease termination, vacancy costs and termination costs associated with headcount reduction.

The Company's restructuring actions include one-time involuntary termination benefits as well as certain contractual termination benefits or employee terminations under ongoing benefit arrangements. One-time involuntary termination benefits are recognized as a liability at estimated fair value when the plan of termination has been communicated to employees and certain other criteria are met. Ongoing termination benefit arrangements are recognized as a liability at estimated fair value when it is probable that amounts will be paid to employees and such amounts are reasonably estimable. When the Company ceases using a facility but does not intend to or is unable to terminate the operating lease, the Company records a liability for the present value of the remaining lease payments, net of estimated sublease income, if any, that could be reasonably obtained for the property (even if the Company does not intend to sublease the facility for the remaining term of the lease). Costs associated with exit or disposal activities, including the related one-time and ongoing involuntary termination benefits, are included as "Acquisition, integration and restructuring costs" on the consolidated statements of income. See "Note 8—Restructuring Expenses" for additional information about the Company's restructuring activities.

Revenue Recognition

The Company's revenues from contracts with customers are from offerings including enterprise modernization; cyber operations; operations and logistics; mission software systems; integrated systems; sensors and phenomenology; and mission support, primarily with the U.S. government and its agencies. The Company also serves various state and local governments, foreign governments and U.S. commercial customers.

The Company performs under various types of contracts, which include firm-fixed-price ("FFP"), time-and-materials ("T&M"), fixed-price-level-of-effort ("FP-LOE"), cost-plus-fixed-fee, cost-plus-award-fee, cost-plus-incentive-fee and fixed-price-incentive-fee ("FP-IF") contracts.

To determine the proper revenue recognition, the Company first evaluates whether it has a duly approved and enforceable contract with a customer, in which the rights of the parties and payment terms are identified, and collectability is probable. The Company also evaluates whether two or more contracts should be combined and accounted for as a single contract, including the task orders issued under an indefinite delivery/indefinite quantity ("IDIQ") award. In addition, the Company assesses contract modifications to determine whether changes to existing contracts should be accounted for as part of the original contract or as a separate contract. Contract modifications for the Company generally relate to changes in contract specifications and requirements and do not add distinct services, and therefore are accounted for as part of the original contract. If contract modifications add distinct goods or services and increase the contract value by an amount that reflects the standalone selling price, those modifications are accounted for as separate contracts.

Most of the Company's contracts are comprised of multiple promises including the design and build of software-based systems, integration of hardware and software solutions, running and maintaining of IT infrastructure and procurement services. In all cases, the Company assesses if the multiple promises should be accounted for as separate performance obligations or combined into a single performance obligation. The Company generally separates multiple promises in a contract as separate performance obligations if those promises are distinct, both individually and in the context of the contract. If multiple promises in a contract are highly interrelated or require significant integration or customization within a group, they are combined and accounted for as a single performance obligation.

The Company's contracts with the U.S. government often contain options to renew existing contracts for an additional period of time (generally a year at a time) under the same terms and conditions as the original contract, and generally do not provide the customer any material rights under the contract. The Company accounts for renewal options as separate contracts when they include distinct goods or services at standalone selling prices.

Contracts with the U.S. government are subject to the Federal Acquisition Regulation ("FAR") and priced on estimated or actual costs of providing the goods or services. The FAR provides guidance on types of costs that are allowable in establishing prices for goods and services provided to the U.S. government and its agencies. Each contract is competitively priced and bid separately. Pricing for non-U.S. government agencies and commercial customers is based on specific negotiations with each customer. In circumstances where the standalone selling price is not directly observable, we estimate the standalone selling price using the expected cost plus margin approach. The Company excludes any taxes collected or imposed when determining the transaction price.

Certain of the Company's cost-plus and fixed-price contracts contain award fees, incentive fees or other provisions that may either increase or decrease the transaction price. These variable amounts generally are awarded upon achievement of certain performance metrics, program milestones or cost targets and can be based upon customer discretion. The Company estimates variable consideration at the most probable amount that it expects to be entitled to, based on the assessment of the contractual variable fee criteria, complexity of work and related risks, extent of customer discretion, amount of variable consideration received historically and the potential of significant reversal of revenue.

The Company allocates the transaction price of a contract to its performance obligations in the proportion of its respective standalone selling prices. The standalone selling price of the Company's performance obligations is generally based on an expected cost-plus margin approach, in accordance with the FAR. For certain product sales, the Company uses prices from other standalone sales. Substantially all of the Company's contracts do not contain a significant financing component, which would require an adjustment to the transaction price of the contract.

The Company recognizes revenue on its service based contracts primarily over time as there is continuous transfer of control to the customer over the duration of the contract as the Company performs the promised services. For U.S. government contracts, continuous transfer of control to the customer is evidenced by clauses in the contract that allow the customer to unilaterally terminate the contract for convenience, pay for costs incurred plus a reasonable profit and take control of any work-in-process. Similarly, for non-U.S. government contracts, the customer typically controls the work-in-process as evidenced by rights to payment for work performed to date plus a reasonable profit to deliver products or services that do not have an alternate use to the Company. Anticipated losses on service based contracts are recognized when known. In certain product sales, where the products have an alternate use, the Company recognizes revenue at a point in time when the customer takes control of the asset usually denoted by possession and legal title.

On FFP contracts, revenue recognized over time generally uses a method that measures the extent of progress towards completion of a performance obligation, principally using a cost-input method (referred to as the cost-to-cost method). Under the cost-to-cost method, revenue is recognized based on the proportion of total costs incurred to estimated total costs-at-completion ("EAC"). A performance obligation's EAC includes all direct costs such as materials, labor, subcontract costs, overhead, and a ratable portion of general and administrative costs. In addition, the Company includes in an EAC of a performance obligation future losses estimated to be incurred on onerous contracts, as and when known. On certain other contracts, principally T&M, FP-LOE, and cost-plus, revenue is recognized using the right-to-invoice practical expedient as the Company is contractually able to invoice the customer based on the control transferred to the customer. Additionally, on maintenance (generally FFP) performance obligations, revenue is recognized over time using a straight-line method as the control of the services is provided to the customer evenly over the period of performance.

For certain performance obligations, the Company is not primarily responsible for fulfilling the promise to provide the goods or service to the customer, does not have inventory risk and does not have discretion in establishing the price for the goods or service. In such cases, the Company recognizes revenue on a net basis.

Contract Costs

Contract costs generally include direct costs such as materials, labor, subcontract costs and indirect costs identifiable with or allocable to a specific contract. Costs are expensed as incurred except for costs incurred to fulfill a contract, which are capitalized and amortized on a straight-line basis over the expected period of performance. The Company does not incur significant incremental costs to acquire contracts. Contract costs incurred for U.S. government contracts, including indirect costs, are subject to audit and adjustment by the Defense Contract Audit Agency ("DCAA") (see "Note 25—Contingencies").

Pre-contract Costs

Costs incurred on projects as pre-contract costs are deferred as assets when the Company has been requested by the customer to begin work under a new arrangement prior to contract execution and it is probable that the Company will recover the costs through the issuance of a contract. When the formal contract has been executed, the costs are recorded to the contract and revenue is recognized.

Transition Costs

Under certain service contracts, costs are incurred, usually at the beginning of the contract performance, to transition the services, employees and equipment to or from the customer or prior contractor. These costs are generally capitalized as deferred assets and amortized over the contractual period of performance and unexercised option periods.

Project Assets

Purchases of project assets are capitalized for specific contracts where delivery has not yet occurred, ownership is maintained by the Company over the life of the contract or the benefit is received over a period of time. Project assets include enterprise software licenses, hardware, maintenance agreements, computers and significant material purchases and other costs incurred on contracts. Project assets are relieved from the balance sheet based on different methodologies, including transfer of assets and amortization based on the estimated useful life of the asset or using the straight-line method over the expected term of the performance obligation.

Changes in Estimates on Contracts

Changes in estimates related to contracts accounted for using the cost-to-cost method of accounting are recognized in the period in which such changes are made for the inception-to-date effect of the changes, with the exception of contracts acquired through the acquisition of the IS&GS Business (see "Note 6—Acquisitions"), where the adjustment is for the period commencing from the date of acquisition.

Table of Contents
LEIDOS HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Changes in estimates on contracts for the periods presented were as follows:

	Year Ended		
	December 28, 2018	December 29, 2017	December 30, 2016
	(in millions, except for per share amounts)		
Net favorable impact to income before income taxes	$105	$ 103	$ 37
Impact on diluted EPS attributable to Leidos common stockholders	$0.52	$ 0.41	$ 0.22

The increase in the changes in estimates on contracts from fiscal 2016 to fiscal 2017 is primarily due to completion of contracts or events which mitigated risk and due to the finalization of award and incentive fees.
The impact on diluted EPS attributable to Leidos common stockholders is calculated using the Company's statutory tax rate.
During fiscal 2018, revenue recognized from performance obligations satisfied in previous periods was $102 million. The changes primarily relate to revisions of variable consideration, including award fees, and revisions to estimates at completion resulting from changes in contract scope, mitigation of contract risks or due to true-ups of contract estimates at the end of contract performance.

Selling, General and Administrative Expenses

The Company classifies indirect costs incurred within or allocated to its U.S. government customers as overhead (included in "Cost of revenues") or general and administrative expenses in the same manner as such costs are defined in the Company's disclosure statements under U.S. government CAS.
Selling, general and administrative expenses include general and administrative, bid and proposal and internal research and development ("IR&D") expenses.
The Company conducts research and development activities under customer-funded contracts and with company-funded IR&D funds. For fiscal 2018, 2017 and 2016, company-funded IR&D expense was $46 million, $42 million and $44 million, respectively. Expenses for research and development activities performed under customer contracts are charged directly to cost of revenues for those contracts.

Income Taxes

The Company accounts for income taxes under the asset and liability method in accordance with the accounting standard for income taxes. The asset and liability method requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and tax bases of assets and liabilities. Under this method, changes in tax rates and laws are recognized in income in the period such changes are enacted.
The Company records net deferred tax assets to the extent that it believes these assets will more likely than not be realized. In making such determination, the Company considers all available positive and negative evidence, including future reversals of existing taxable temporary differences, projected future taxable income, tax planning strategies and recent results of operations. If the Company were to determine that it would be able to realize its deferred income tax assets in the future in excess of their net recorded amount or would no longer be able to realize its deferred income tax assets in the future as currently recorded, the Company would make an adjustment to the valuation allowance which would decrease or increase the provision for income taxes.
The provision for federal, state, foreign and local income taxes is calculated on income before income taxes based on current tax law and includes the cumulative effect of any changes in tax rates from those used previously in determining deferred tax assets and liabilities. Such provision differs from the amounts currently payable because certain items of income and expense are recognized in different reporting periods for financial reporting purposes than for income tax purposes.

The Company recognizes liabilities for uncertain tax positions when it is more likely than not that a tax position will not be sustained upon examination and settlement with various taxing authorities. Liabilities for uncertain tax positions are measured based upon the largest amount of benefit that is greater than 50% likely of being realized upon ultimate settlement. The Company recognizes interest and penalties related to uncertain tax positions in its income tax expense.

Cash and Cash Equivalents

The Company's cash equivalents were primarily comprised of investments in several large institutional money market funds and bank deposits, with original maturity of three months or less. The Company includes outstanding payments within "Cash and cash equivalents" and correspondingly increases "Accounts payable and accrued liabilities" on the consolidated balance sheets. At December 28, 2018, and December 29, 2017, the Company included $56 million and $169 million, respectively, of outstanding payments within "Cash and cash equivalents."

Restricted Cash

The Company has restricted cash balances, primarily representing advances from customers that are restricted as to use for certain expenditures related to that customer's contract. Restricted cash balances are included as "Other current assets" in the consolidated balance sheets.

Receivables

The Company's receivables include amounts billed and currently due from customers, amounts billable where the right to consideration is unconditional and amounts unbilled. As of fiscal 2018, amounts billable were classified as billed receivables. These receivables were classified as unbilled receivables for fiscal 2017 (see "Note 9—Receivables"). Amounts billable and unbilled amounts are recognized at estimated realizable value and consist of costs and fees, substantially all of which are expected to be billed and collected generally within one year. Unbilled amounts also include rate variances that are billable upon negotiation of final indirect rates with the DCAA.

The typical billing for the Company's cost-reimbursable and T&M contracts is as costs are incurred. FFP contracts are billed either based on milestones, which are the achievement of specific events as defined in the contract, or based on progress payments, which are interim payments up to a designated amount of costs incurred as work progresses. On certain contracts, the customer withholds a certain percentage of the contract price (retainage). These withheld amounts are included within the Company's unbilled receivables and are billed upon contract completion or the occurrence of a specified event, and when negotiation of final indirect rates with the U.S. government is complete. Based on the Company's historical experience, the write-offs of retention balances have not been significant.

When events or conditions indicate that amounts outstanding from customers may become uncollectible, an allowance is estimated and recorded.

Amounts billed and collected on contracts but not yet recorded as revenue because the Company has not performed its obligation under the arrangement with a customer are deferred and included within "Accounts payable and accrued liabilities" or "Other long-term liabilities" on the consolidated balance sheets.

Concentration of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk primarily consist of accounts receivable and derivatives. Since the Company's receivables are primarily with the U.S. government, the Company does not have exposure to a material credit risk. The Company manages its credit risk related to derivatives through the use of multiple counterparties with high credit standards.

Inventories

Inventories are valued at the lower of cost or estimated net realizable value. Raw material inventory is valued using the average cost method. Work-in-process inventory includes raw material costs plus labor costs, including fringe benefits and allocable overhead costs. The majority of finished goods inventory consists of security products, inspection systems and baggage scanning equipment. The Company evaluates inventory against historical and planned usage to determine appropriate provisions for obsolete inventory. Inventory balances are included as "Other current assets" in the consolidated balance sheets.

Goodwill

Goodwill represents the excess of the fair value of consideration transferred, plus the fair value of any non-controlling interests in the acquiree, over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. Goodwill is not amortized, but instead is tested annually for impairment at the reporting unit level and tested more frequently if events or circumstances indicate that the carrying value may not be recoverable. The Company's policy is to perform its annual goodwill impairment evaluation as of the first day of the fourth quarter of its fiscal year. During fiscal 2018, the Company had five reporting units for the purpose of testing goodwill for impairment.

Goodwill is evaluated for impairment either under a qualitative assessment option or a quantitative approach depending on the facts and circumstances of a reporting unit, consideration of the excess of a reporting unit's fair value over its carrying amount in previous assessments and changes in business environment.

When performing a qualitative assessment, the Company considers factors including, but not limited to, current macroeconomic conditions, industry and market conditions, cost factors, financial performance and other events relevant to the entity or reporting unit under evaluation to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If the Company determines that it is more likely than not that a reporting unit's fair value is less than its carrying amount, a quantitative goodwill impairment test is performed.

When performing a quantitative goodwill impairment test, the reporting unit carrying value is compared to its fair value. Goodwill is deemed impaired if, and the impairment loss is recognized for the amount by which, the reporting unit carrying value exceeds its fair value.

The Company estimates the fair value of each reporting unit using both market and income approaches (Level 3) when a quantitative analysis is performed. To determine the fair value of the reporting units, the outputs from both methods are equally weighted.

The market approach is a technique where the fair value is calculated based on the multiples of comparable publicly-traded companies that provide a reasonable basis of comparison with each of the Company's reporting units. Valuation ratios are selected that relate market prices to selected financial metrics from comparable companies. These ratios are applied after consideration of adjustments and weightings related to financial position, growth, volatility, working capital movement and other factors. Due to the fact that stock prices of comparable companies represent minority interests, the Company also considers an acquisition control premium to reflect the impact of additional value associated with a controlling interest.

The income approach is a technique where the fair value is calculated based on present value of future cash flows using risk-adjusted discount rates, which represent the weighted-average cost of capital ("WACC") for each reporting unit. Determination of WACC includes assessing the cost of equity and debt as of the valuation date. In addition, a terminal value is developed for forecasted future cash flows beyond the projection period discounted back to the present value. The forecasts used in the Company’s estimation of fair value are developed by management based on business and market considerations.

The goodwill impairment test process and valuation model is based upon certain key assumptions that require the exercise of significant judgment and assumptions including the use of appropriate financial projections, economic expectations, WACC and expected long-term growth rates, as well as using available market data. Significant changes to these estimates and assumptions could adversely impact conclusions and actual future results may differ from the estimates. In addition, the identification of reporting units and the allocation of assets and liabilities to the reporting units when determining the carrying value of each reporting unit also requires judgment.

Intangible Assets

Acquired intangible assets with finite lives and internally developed software are amortized using the method that best reflects how their economic benefits are utilized or, if a pattern of economic benefits cannot be reliably determined, on a straight-line basis over their estimated useful lives. Intangible assets with finite lives are amortized over the following periods:

	Estimated useful lives (in years)
Program and contract intangibles	6-11
Backlog	1
Customer relationships	8
Software and technology	4-15

Intangible assets with finite lives are assessed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

Intangible assets with indefinite lives are not amortized but are assessed for impairment at the beginning of the fourth quarter and whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

Property, Plant and Equipment

Purchases of property, plant and equipment, including purchases of software and software licenses, as well as costs associated with major renewals and improvements are capitalized. Maintenance, repairs and minor renewals and improvements are expensed as incurred.

Construction in Progress ("CIP") is used to accumulate all costs for projects that are not yet complete. CIP balances are transferred to the appropriate asset account when the asset is capitalized and ready for its intended use.

When assets are sold or otherwise disposed of, the cost and related accumulated depreciation or amortization are removed from the accounts and any resulting gain or loss is recognized. Depreciation is recognized using the methods and estimated useful lives as follows:

	Depreciation method	Estimated useful lives (in years)
Computers and other equipment	Straight-line or declining-balance	3-10
Buildings	Straight-line	Not to exceed 40
Building improvements and leasehold improvements	Straight-line	Shorter of useful life of asset or remaining lease term
Office furniture and fixtures	Straight-line or declining-balance	6-9

The Company evaluates its long-lived assets for potential impairment whenever there is evidence that events or changes in circumstances indicate that the carrying value may not be recoverable and the carrying amount of the asset exceeds its estimated fair value.

Fair Value Measurements

The accounting standard for fair value measurements establishes a three-level fair value hierarchy, which prioritizes the inputs used in measuring fair value as follows: observable inputs such as quoted prices in active markets (Level 1); inputs other than quoted prices in active markets for identical assets or liabilities that are observable either directly or indirectly or quoted prices that are not active (Level 2); and unobservable inputs in which there is little or no market data (e.g., discounted cash flow and other similar pricing models), which requires the Company to develop its own assumptions (Level 3).

Table of Contents

The accounting guidance for fair value measurements requires that the Company maximize the use of observable inputs and minimize the use of unobservable inputs in determining fair value. The accounting guidance provides for the irrevocable option to elect, on a contract-by-contract basis, to measure certain financial assets and liabilities at fair value at inception of the contract and record any subsequent changes in fair value in earnings. The Company has not made fair value option elections on any of its financial assets and liabilities.

The fair value of financial instruments is determined based on quoted market prices, if available, or management's best estimate (see "Financial Instruments" below).

Management evaluates its investments for other-than-temporary impairment at each balance sheet date. When testing long-term investments for recovery of carrying value, the fair value of long-term investments is determined using various valuation techniques and factors such as, market prices of comparable companies (Level 2 input), discounted cash flow models (Level 3 input) and recent capital transactions of the portfolio companies being valued (Level 3 input). If management determines that an other-than-temporary decline in the fair value of an investment has occurred, an impairment loss is recognized to reduce the investment to its estimated fair value.

The Company's non-financial instruments measured at fair value on a non-recurring basis include goodwill, indefinite-lived intangible assets and long-lived tangible assets. The valuation methods used to determine fair value require a significant degree of management judgment to determine the key assumptions. As such, the Company generally classifies non-financial instruments as either Level 2 or Level 3 fair value measurements.

Financial Instruments

The Company is exposed to certain market risks which are inherent in certain transactions entered into during the normal course of business. These transactions include sales or purchase contracts denominated in foreign currencies and exposure to changing interest rates. The Company manages its risk to changes in interest rates through the use of derivative instruments.

For fixed rate borrowings, the Company uses variable interest rate swaps, effectively converting fixed rate borrowings to variable rate borrowings. These swaps are designated as fair value hedges. The fair value of these interest rate swaps is determined based on observed values for underlying interest rates on the LIBOR yield curve (Level 2).

For variable rate borrowings, the Company uses fixed interest rate swaps, effectively converting a portion of the variable interest rate payments to fixed interest rate payments. These swaps are designated as cash flow hedges. The fair value of these interest rate swaps is determined based on observed values for the underlying interest rates (Level 2).

The Company does not hold derivative instruments for trading or speculative purposes.

The Company's defined benefit plan assets consist of investments in pooled funds that contain investments with values based on quoted market prices, but for which the pools are not valued on a daily quoted market basis (Level 2).

Stock-Based Compensation

The Company accounts for stock-based compensation at the grant date based on the fair value of the award and is recognized as expense over the requisite service period, which is generally the vesting period, net of an estimated forfeiture rate.

The fair value of restricted stock awards and performance-based stock awards is based on the closing price of the Company's common stock on the date of grant. The fair value of performance-based stock awards with market conditions is based on using the Monte Carlo simulation.

The fair value of stock option awards granted is based on using the Black-Scholes-Merton option pricing model. The estimation of stock option fair value requires management to make estimates and judgments about, among other things, employee exercise behavior, forfeiture rates and the expected volatility of Leidos common stock over the expected option term. These judgments directly affect the amount of compensation expense that will ultimately be recognized.

Foreign Currency

The financial statements of consolidated international subsidiaries, for which the functional currency is not the U.S. dollar, are translated into U.S. dollars using the exchange rate at each balance sheet date for assets and liabilities and a weighted average exchange rate over the reporting period for revenues, expenses, gains and losses. Translation adjustments are recorded as accumulated other comprehensive (loss) income in stockholders' equity. Gains and losses due to movements in foreign currency exchange rates are recognized as "Other expense, net" on the consolidated statements of income.

Note 4—Revenues

Dual Reporting

The effects to the consolidated financial statements at and as of December 28, 2018, as a result of applying ASC 606, rather than previous GAAP ("ASC 605"), were the following:

Balance Sheet

	As Reported (ASC 606)	As Adjusted (ASC 605)
	(in millions)	
Receivables, net	$1,877	$ 1,872
Other current assets	543	545
Accumulated earnings (deficit)	372	369

Income Statement

	Year Ended December 28, 2018	
	As Reported (ASC 606)	As Adjusted (ASC 605)
	(in millions)	
Revenues	$10,194	$ 10,189
Cost of revenues	8,690	8,688
Operating income	749	746

The changes reflected above were primarily due to the Company's units-of-delivery contracts, which were recognized at a point in time under ASC 605 and are recognized using an over-time model under ASC 606.

Remaining Performance Obligations

Remaining performance obligations represent the expected value of exercised contracts, both funded and unfunded, less revenue recognized to date. Remaining performance obligations do not include unexercised option periods and future potential task orders expected to be awarded under IDIQ contracts.

As of December 28, 2018, the Company had $10.2 billion of remaining performance obligations, which are expected to be recognized as revenue in the amounts of $7.3 billion, $1.1 billion and $1.8 billion for fiscal 2019, fiscal 2020 and fiscal 2021 and thereafter, respectively.

Disaggregation of Revenues

The Company disaggregates revenues by customer-type, contract-type and geographic location for each of its reportable segments. These categories represent how the nature, timing and uncertainty of revenues and cash flows are affected by the U.S. government procurement environment.

Disaggregated revenues by customer-type were as follows:

	Year Ended December 28, 2018			
	Defense Solutions	Civil	Health	Total
	(in millions)			
DoD	$4,318	$128	$386	$4,832
Other government agencies[1]	194	2,412	1,276	3,882
Commercial and non-U.S. customers	436	889	155	1,480
Total	$4,948	$3,429	$1,817	$10,194

[1] Includes non-DoD federal government agencies, state and local government agencies.

The majority of the Company's revenues are generated from U.S. government contracts, either as a prime contractor or as a subcontractor to other contractors. Revenues from the U.S. government can be adversely impacted by spending caps or changes in budgetary priorities of the U.S. government, as well as delays in program start dates or the award of a contract. Government spending levels for the DoD may be impacted by spending priorities as a result of competing demands for federal funds.

Disaggregated revenues by contract-type were as follows:

	Year Ended December 28, 2018			
	Defense Solutions	Civil	Health	Total
	(in millions)			
Cost-reimbursement and fixed-price-incentive-fee	$3,417	$1,863	$189	$5,469
Firm-fixed-price	1,031	1,004	1,134	3,169
Time-and-materials and fixed-price-level-of-effort	500	562	494	1,556
Total	$4,948	$3,429	$1,817	$10,194

Cost-reimbursement and FP-IF contracts are generally lower risk and have lower profits. T&M and FP-LOE contracts are also low risk but profits may vary depending on actual labor costs compared to negotiated contract billing rates. FFP contracts offer the potential for higher profits while increasing the Company’s exposure to risk of cost overruns.

Disaggregated revenues by geographic location were as follows:

	Year Ended December 28, 2018			
	Defense Solutions	Civil	Health	Total
	(in millions)			
United States	$4,572	$2,876	$1,817	$9,265
International	376	553	—	929
Total	$4,948	$3,429	$1,817	$10,194

The Company's international business operations, primarily located in Australia and the U.K., are subject to additional and different risks than its U.S. business. Failure to comply with U.S. government laws and regulations applicable to international business, such as the Foreign Corrupt Practices Act or U.S. export control regulations, could have an adverse impact on the Company's business with the U.S. government.

In some countries, there is an increased chance for economic, legal or political changes that may adversely affect the performance of the Company's services, sales of products or repatriation of profits. International transactions can also involve increased financial and legal risks arising from foreign exchange variability, imposition of tariffs or additional taxes and restrictive trade policies and delays or failure to collect amounts due to differing legal systems.

Note 5—Contract Assets and Liabilities
The Company's performance obligations are satisfied either over time as work progresses or at a point in time. FFP contracts are typically billed to the customer using milestone payments while cost-reimbursable and T&M contracts are typically billed to the customer on a monthly or bi-weekly basis as indicated by the negotiated billing terms and conditions of the contract. As a result, for each of the company's contracts, the timing of revenue recognition, customer billings and cash collections results in a net contract asset or liability at the end of each reporting period.
Contract assets include unbilled receivables, which is the amount of revenue recognized that exceeds the amount billed to the customer, where right to payment is not just subject to the passage of time.
Contract liabilities consist of deferred revenue.
The components of contract assets and contract liabilities consisted of the following:

	Balance sheet line item	December 28, 2018	December 30, 2017[1]
		(in millions)	
Contract assets - current:			
Unbilled receivables[2]	Receivables, net	$ 818	$ 844
Contract liabilities - current:			
Deferred revenue	Accounts payable and accrued liabilities	$ 276	$ 293
Contract liabilities - non-current:			
Deferred revenue	Other long-term liabilities	$ 10	$ 17

[1] Includes the cumulative effect of the changes made to the Company's opening balance sheet at December 30, 2017, as a result of the adoption of ASU 2014-09, Revenue from Contracts with Customers (Topic 606).
[2] Balances exclude $381 million and $234 million determined to be billable at December 28, 2018, and December 30, 2017, respectively.
The decrease in unbilled receivables was primarily due to the timing of billings and revenue recognized on certain contracts. The decrease in deferred revenue was primarily due to revenue recognized during the period partially offset by the timing of advance payments from customers.
During fiscal 2018, the Company recognized revenues of $208 million relating to amounts that were included as a contract liability at December 30, 2017.
The Company did not recognize any impairment losses on contract assets during fiscal 2018.
Note 6—Acquisitions
The Company may acquire businesses as part of its growth strategy to provide new or enhance existing capabilities and offerings to customers. During fiscal 2016, the Company completed the acquisition of Lockheed Martin's IS&GS Business.
Lockheed Martin Transaction
On January 26, 2016, Leidos announced it had entered into a definitive agreement (as amended, the "Merger Agreement") with Lockheed Martin Corporation ("Lockheed Martin"); Abacus Innovations Corporation, a Delaware corporation and a wholly owned subsidiary of Lockheed Martin ("Splitco"); and Lion Merger Co., a Delaware corporation and, at the time of announcement, a wholly owned subsidiary of Leidos ("Merger Sub"), pursuant to which Leidos would combine with Lockheed Martin's realigned Information Systems & Global Solutions business in a Reverse Morris Trust transaction. In connection with the Merger Agreement, Lockheed Martin and Splitco entered into a Separation Agreement dated January 26, 2016 (as amended, the "Separation Agreement"), pursuant to which

Lockheed Martin would separate the IS&GS Business from Lockheed Martin and transfer the IS&GS Business to Splitco. The transactions contemplated by the Merger Agreement and the Separation Agreement are referred to herein as the "Transactions."

On August 16, 2016, the acquisition date, the Company completed the Transactions. In the Transactions, among other steps, (i) Lockheed Martin transferred the IS&GS Business to Splitco; (ii) Lockheed Martin offered to Lockheed Martin stockholders the right to exchange all or a portion of their shares of Lockheed Martin common stock for shares of Splitco common stock by way of an exchange offer (the "Distribution"); and (iii) Merger Sub merged with and into Splitco, with Splitco as the surviving corporation (the "Merger") and a wholly owned subsidiary of Leidos. Upon consummation of the Transactions, those Lockheed Martin stockholders who elected to participate in the exchange offer received approximately 77 million shares of Leidos common stock, which represented approximately 50.5% of the outstanding shares of Leidos common stock after consummation of the Transactions. Holders of Leidos shares prior to the transaction held the remaining 49.5% of the outstanding shares of Leidos common stock immediately after the closing.

Prior to the Distribution, Splitco incurred third-party debt financing in an aggregate principal amount of $1.8 billion and immediately thereafter, Lockheed Martin transferred the IS&GS Business to Splitco and Splitco made a special cash payment to Lockheed Martin of $1.8 billion.

In connection with the Transactions, Leidos incurred new indebtedness and assumed Splitco's indebtedness in the form of term loans in an aggregate principal amount of $690 million and $1.8 billion, respectively, and entered into a new $750 million senior secured revolving credit facility, which replaced its existing revolving credit facility. See "Note 15—Debt" for further information regarding the debt incurred and the senior revolving credit facility.

In conjunction with the Transactions, Leidos' Board of Directors declared a special dividend of $13.64 per share of Leidos common stock. Consequently, on August 22, 2016, the Company paid $993 million to stockholders of record as of August 15, 2016, and accrued $29 million of dividend equivalents with respect to outstanding equity awards. See "Note 19—Stock-Based Compensation" for further information regarding the modifications made to the Company's outstanding stock awards as a result of the special dividend.

As a result of the Transactions, membership on the Leidos Board of Directors was increased to 12 directors, in which three directors designated by Lockheed Martin were appointed to the board. A majority of the senior management of Leidos immediately prior to the consummation of the Transactions remained Leidos executive officers immediately after the Transactions. Leidos management determined that Leidos is the accounting acquirer in the Transactions based on the facts and circumstances noted within this section and other relevant factors.

The acquisition adds large, complex information technology ("IT") system implementation and operation experience and additional federal and international IT solutions and services work to the Leidos portfolio, providing more venues to sell value added services such as cybersecurity and analytics. As a result, the Company is more diversified in markets it serves and provides the Company the scale and access to markets intended to further growth.

The final purchase consideration for the acquisition of the IS&GS Business was as follows (in millions):

Value of common stock issued to Lockheed Martin stockholders[1]	$2,929
Equity consideration for replacement awards[2]	9
Working capital adjustments[3]	81
Purchase price	$3,019

[1] Represents approximately 77 million new shares of Leidos common stock issued to those Lockheed Martin stockholders who elected to participate in the exchange offer, based on the Company's August 16, 2016, closing share price of $51.69, less the Leidos special cash dividend amount of $13.64, which the Lockheed Martin stockholders were not entitled to receive.

[2] Represents a portion of the $23 million total fair value of replacement equity-based awards attributable to the pre-Merger service period. The remaining $12 million, net of estimated forfeitures, will be recognized as stock-based compensation expense over the remaining requisite service period (see "Note 19—Stock-Based Compensation").

(3) In January 2018, the Company finalized its net working capital at $105 million. The additional $24 million was recorded as acquisition costs in the consolidated statements of income.

Table of Contents

The final fair values of the assets acquired and liabilities assumed at the date of the Transactions were as follows (in millions):

Cash	$25
Receivables, net	938
Other current assets	73
Property, plant and equipment	87
Intangible assets	1,194
Other assets	58
Accounts payable and accrued liabilities	(733)
Accrued payroll and employee benefits	(186)
Long-term debt, current portion	(23)
Deferred tax liabilities	(328)
Long-term debt, net of current portion	(1,780)
Other long-term liabilities	(45)
Total identifiable net liabilities assumed	(720)
Non-controlling interest	(13)
Goodwill	3,752
Purchase price	$3,019

During fiscal 2017, the Company recorded adjustments to finalize the fair value of acquired assets and liabilities assumed which resulted in a $337 million increase in goodwill. Significant changes included intangible assets, property, plant and equipment, deferred tax assets, other assets, accounts payable and accrued liabilities and deferred tax liabilities. The Company recognized cumulative catch-up adjustments related to valuation adjustments for equity method investments and property, plant, and equipment, which resulted in an increase of $7 million in amortization expense and an increase of $7 million of depreciation expense, respectively. The Company recorded the cumulative catch-up adjustments to equity method investments within "Equity earnings of non-consolidated subsidiaries" and adjustments to depreciation within "Costs of revenues" and "Selling, general and administrative expenses" on the consolidated statement of income.

Additionally, during fiscal 2017, the Company recorded a valuation adjustment to reflect the fair value of the non-controlling interest acquired. The fair value of $13 million was determined by calculating the present value of future cash flows for the non-controlling interest. Significant assumptions inherent in the valuation of the non-controlling interest include the estimated after-tax cash flows expected to be received and an assessment of the appropriate discount rate.

The goodwill represents intellectual capital and the acquired assembled work force, none of which qualify for recognition as a separate intangible asset. The value of goodwill has been allocated to the reporting units on a relative fair value approach (see "Note 10—Goodwill"). Of the total goodwill, $414 million is tax deductible.

The Company identified $1.2 billion of intangible assets, representing program and contract intangibles, backlog and software and technology. The fair value measurements were primarily based on significant inputs that are not observable in the market and represent a Level 3 measurement (see "Note 13—Fair Value Measurements"). The income approach was primarily used to value the intangible assets, consisting primarily of acquired program and contract intangibles and backlog. The income approach indicates value for an asset based on the present value of cash flow projected to be generated by the asset. Projected cash flow is discounted at a rate of return that reflects the relative risk of achieving the cash flow and the time value of money.

The following table summarizes the fair value of intangible assets acquired at the date of acquisition and the related weighted average amortization period:

	Weighted average amortization period	Fair value
	(in years)	(in millions)
Program and contract intangibles[1]	9.7	$ 1,011
Backlog	1.8	157
Software and technology[1]	4.6	26
Total	8.6	$ 1,194

[1] The weighted average amortization period is estimated based on the projected economic benefits associated with these assets.

The Company incurred the following expenses related to the acquisition and integration of the IS&GS Business:

	Year Ended December 28, 2018	December 29, 2017	December 30, 2016
	(in millions)		
Acquisition costs	$—	$ 25	$ 44
Integration costs	29	77	46
Total acquisition and integration costs	$29	$ 102	$ 90

These acquisition and integration costs have been recorded within Corporate and presented in "Acquisition, integration and restructuring costs" on the consolidated statements of income.

On January 10, 2018, the final amount of the net working capital of the IS&GS Business was determined through a binding arbitration proceeding in accordance with the Separation Agreement with Lockheed Martin. As a result, $24 million was recorded as acquisition costs in the consolidated statements of income for fiscal 2017. On January 18, 2018, the final working capital amount of $105 million was paid to Lockheed Martin, of which $24 million and $81 million was presented as cash flows from operating and investing activities, respectively, on the consolidated statement of cash flows.

During fiscal 2018, a tax indemnification liability of $23 million was paid to Lockheed Martin in accordance with the Tax Matters Agreement, which was presented as cash flows from financing activities on the consolidated statement of cash flows.

Pro Forma Financial Information (unaudited)

The following pro forma financial information presents consolidated results of operations as if the acquisition had occurred on January 31, 2015. The pro forma financial information was prepared based on historical financial information and has been adjusted to give effect to the events that are directly attributable to the Transactions and factually supportable. The pro forma results below do not reflect future events that have occurred or may occur after the Transactions, including anticipated synergies or other expected benefits that may be realized from the Transactions. The pro forma financial information is not intended to reflect the actual results of operations that would have occurred if the acquisition had been completed on January 31, 2015, nor is it intended to be an indication of future operating results.

Table of Contents
LEIDOS HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)	Year Ended December 30, 2016 (in millions, except for per share amounts)
Revenues	$ 10,443
Net income	340
Net income attributable to Leidos common stockholders	335
Earnings per share:	
Basic	$ 2.23
Diluted	2.20

The unaudited pro forma financial information above excludes acquisition-related costs of $44 million as a non-recurring significant adjustment. This adjustment was made to account for certain costs incurred as if the Transactions had been completed on January 31, 2015.

Note 7—Divestitures

Commercial Cybersecurity Business

On June 5, 2018, the Company entered into a Stock and Asset Purchase Agreement to sell the Company's commercial cybersecurity business, included within the Company's Civil segment, in order to focus on providing solutions, including cybersecurity, to the Company's core markets of governments and highly regulated industries. The sale is expected to be completed in early fiscal 2019 and is not expected to result in a loss. The Company has presented the associated assets and liabilities of the business as held for sale in the Company's consolidated balance sheet as of December 28, 2018. The major classes of assets and liabilities classified as held for sale were as follows:

	December 28, 2018 (in millions)
Receivables, net	$ 16
Other current assets	5
Property, plant and equipment, net	3
Intangible assets, net	5
Goodwill	57
Deferred tax assets	6
Total assets held for sale	$ 92
Accounts payable and accrued liabilities	$ 16
Accrued payroll and employee benefits	4
Other long-term liabilities	3
Total liabilities held for sale	$ 23

The planned disposition does not represent a strategic shift in operations that will have a material effect on the Company's operations and financial results, and accordingly was not presented as discontinued operations.

Heavy Construction Business

In April 2016, the Company's Civil segment disposed of a business that was primarily focused on providing design, build and heavy construction engineering services. The Company received cash proceeds of $23 million, resulting in a pre-tax gain on sale of $3 million. The major classes of assets and liabilities sold included $73 million of accounts receivable, net; $3 million of non-current assets and $63 million of accounts payable and accrued liabilities. The Company recorded the pre-tax gain on sale in "Other expense, net" on the consolidated statements of income.

Plainfield Renewable Energy Holdings LLC

On July 24, 2015, the Company completed the sale of its equity interests in Plainfield Renewable Energy Holdings LLC ("Plainfield"), a biomass-fueled power plant in Plainfield, Connecticut (the "plant"), for an aggregate consideration of $102 million, subject to certain adjustments. The consideration received at closing consisted of a cash payment of $29 million (the "Closing Payment") and a secured promissory note for $73 million, net of discount (the "Note").

The original maturity date of the Note was July 24, 2017 (the "Original Maturity Date"), with an option to extend the maturity date for three consecutive one-year periods. The annual interest rate of 6% would increase to 8% if the maturity date was extended beyond July 24, 2017, and would increase to 9% if extended beyond July 24, 2019. The first payment of accrued and unpaid interest was due January 24, 2016, with subsequent payments occurring every six months, including a portion of the principal balance. The Note allowed for a six-month deferral of certain payments due in January 2016 and July 2016. In January 2016 and July 2016, the Company was notified by the buyer that the interest payment due on January 24, 2016, would be deferred to the next payment date, and a portion of the principal payment due on July 24, 2016, would be deferred to the next payment due date.

During the quarter ended June 30, 2017, Plainfield exercised the first of three one-year term extension options available under the original credit agreement, thereby extending the maturity date of the Note to July 24, 2018. Concurrent with this extension, the interest rate on the Note increased from 6% to 8%. Also, during the quarter ended June 30, 2017, Leidos and Plainfield entered into an amendment to the Note allowing Plainfield to defer up to $4 million of the interest and principal payments due in July 2017 and January 2018 until July 2018. In consideration of this deferment, Leidos received certain concessions and releases from obligations under the original transaction documents.

The Company collected $6 million of principal and interest each year during fiscal 2016 and fiscal 2017. Payments under the Note were secured by a general security interest in the personal property of Plainfield, a pledge of the membership interests of Plainfield and a first mortgage on the real property that comprised the plant.

In January 2018, the Company entered into negotiations with the equity owners of Plainfield LLC regarding the Plainfield Recapitalization Plan ("Plan"). The Plan envisioned raising new equity combined with reduction of Plainfield's debt. As a result, the Company recorded a $33 million impairment of its Note, which is presented in "Other expense, net" on the consolidated statements of income. The net realizable value of the Note at December 29, 2017, was estimated to be approximately $40 million, compared to its carrying value of $73 million, including accrued interest.

On July 12, 2018, Leidos and Plainfield entered into an additional amendment to the Note, allowing Plainfield to defer the maturity of the Note until the earlier of August 24, 2018, or the date Plainfield successfully closed on a refinancing agreement with a third party. Under the terms of the agreement, if Plainfield successfully refinanced the Note prior to August 24, 2018, Leidos would allow Plainfield to settle the Note in full for $40 million plus 50% of additional net proceeds obtained by Plainfield. On August 23, 2018, Leidos and Plainfield entered into an agreement with respect to the final payoff of the Note. As a result, the Company received proceeds of $40 million in full satisfaction of

Plainfield's obligations under the Note.

Table of Contents
LEIDOS HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 8—Restructuring Expenses

After the acquisition of the IS&GS Business, the Company began an initiative to reduce its cost structure, which includes optimization of its real estate portfolio by vacating certain facilities and consolidating others, and by reducing headcount.

The restructuring expenses related to this program were as follows:

	Year Ended December 28, 2018	December 29, 2017	December 30, 2016
	(in millions)		
Severance costs	$ 2	$ 18	$ 10
Lease termination expenses	6	19	2
Restructuring expenses related to the IS&GS Business	$ 8	$ 37	$ 12

As of December 28, 2018, the Company has recognized a total of $57 million of expense in connection with restructuring activities. These restructuring expenses have been recorded within Corporate and presented in "Acquisition, integration and restructuring costs" on the consolidated statements of income.

The related restructuring liability related to this program was as follows:

	Severance Costs	Lease Termination Expenses	Total
	(in millions)		
Balance at December 30, 2016	$ 7	$ 1	$ 8
Charges	18	19	37
Cash payments	(20)	(16)	(36)
Balance at December 29, 2017	5	4	9
Charges	2	6	8
Cash payments	(7)	(8)	(15)
Balance at December 28, 2018	$ —	$ 2	$ 2

Note 9—Receivables

The components of receivables, net consisted of the following:

	December 28, 2018	December 29, 2017
	(in millions)	
Billed receivables[(1)]	$ 1,067	$ 771
Unbilled receivables	818	1,074
Allowance for doubtful accounts	(8)	(14)
	$ 1,877	$ 1,831

[(1)] As a result of the adoption of ASC 606, $381 million of billable receivables were classified as billed receivables for fiscal 2018. $234 million of billable receivables were classified as unbilled receivables for fiscal 2017.

Note 10—Goodwill

During fiscal 2017, the Company completed its business reorganization, which resulted in identification of three reportable segments (Defense Solutions, Civil and Health). Additionally, the Company separately presents the costs associated with corporate functions as Corporate. The Company commenced operating and reporting under the new organizational structure effective the beginning of fiscal 2017 (see "Note 24—Business Segments"). Goodwill, including the amounts from the acquisition of the IS&GS Business, was allocated to the reporting units on a relative fair value approach.

The following table presents changes in the carrying amount of goodwill by reportable segment:

	Defense Solutions	Civil	Health	Total
	(in millions)			
Goodwill at December 30, 2016[(1)]	$1,954	$1,731	$937	$4,622
Adjustment to original purchase price allocation	94	259	(16)	337
Foreign currency translation adjustments	7	8	—	15
Goodwill at December 29, 2017[(1)]	2,055	1,998	921	4,974
Foreign currency translation adjustments	(40)	(11)	—	(51)
Transfers to assets held for sale	—	(57)	—	(57)
Adjustment to goodwill	—	(6)	—	(6)
Goodwill at December 28, 2018[(1)]	$2,015	$1,924	$921	$4,860

[(1)] Carrying amount includes accumulated impairment losses of $369 million and $117 million within the Health and Civil segments, respectively.

See "Note 6—Acquisitions" for the description of adjustments to the original purchase price allocation.

In conjunction with the fiscal 2017 change in reportable segments, the Company evaluated goodwill for impairment, both before and after the segment change and determined that goodwill was not impaired.

Based on a qualitative analysis performed during the Company's annual impairment evaluation for fiscal 2018 and fiscal 2016 for certain of its reporting units, it was determined that it is more likely than not that the fair values of the reporting units were in excess of the individual reporting unit carrying values, and as a result, a quantitative step one analysis was not necessary. Additionally, based on the results of the quantitative step one analysis for certain other of its reporting units, it was determined that the fair value was in excess of the individual reporting units carrying values. In fiscal 2017, the company performed a quantitative analysis for all reporting units. It was determined that the fair values of all reporting units exceeded their carrying values. As a result, no goodwill impairments were identified as part of the annual goodwill impairment evaluation for the periods mentioned above.

During the year ended December 28, 2018, the Company recorded an immaterial correction of $6 million with respect to fair value of liabilities acquired from the Transactions (see "Note 6—Acquisitions").

Note 11—Intangible Assets

Intangible assets consisted of the following:

	December 28, 2018			December 29, 2017		
	Gross carrying value	Accumulated amortization	Net carrying value	Gross carrying value	Accumulated amortization	Net carrying value
	(in millions)					
Finite-lived intangible assets:						
Program and contract intangibles	$1,003	$ (374)	$ 629	$1,013	$ (187)	$ 826
Software and technology	93	(74)	19	89	(64)	25
Customer relationships	4	(4)	—	4	(3)	1
Backlog	—	—	—	158	(158)	—
Total finite-lived intangible assets	1,100	(452)	648	1,264	(412)	852
Indefinite-lived intangible assets:						
Trade names	4	—	4	4	—	4
Total intangible assets	$1,104	$ (452)	$ 652	$1,268	$ (412)	$ 856

Amortization expense related to intangible assets, including those acquired through the Transactions, was $201 million, $281 million and $84 million for fiscal 2018, 2017 and 2016, respectively.

Program and contract intangible assets are amortized over their respective estimated useful lives in proportion to the pattern of economic benefit based on expected future discounted cash flows. Customer relationships and backlog intangible assets are amortized on a straight-line basis over their estimated useful lives. Software and technology intangible assets are amortized either on a straight-line basis over their estimated useful lives or over their respective estimated useful lives in proportion to the pattern of economic benefit based on expected future discounted cash flows, as deemed appropriate.

The estimated annual amortization expense related to finite-lived intangible assets as of December 28, 2018, is as follows:

Fiscal Year Ending	
	(in millions)
2019	$ 171
2020	126
2021	106
2022	92
2023	73
2024 and thereafter	80
	$ 648

Actual amortization expense in future periods could differ from these estimates as a result of future acquisitions, divestitures, impairments, the outcome and timing of completion of in-process research and development projects and other factors.

Note 12—Property, Plant and Equipment

Property, plant and equipment, net consisted of the following:

	December 28, 2018	December 29, 2017
	(in millions)	
Computers and other equipment	$ 233	$ 194
Leasehold improvements	206	171
Buildings and improvements	56	54
Land	40	49
Office furniture and fixtures	36	34
Construction in progress	15	44
	586	546
Less: accumulated depreciation and amortization	(349)	(314)
	$ 237	$ 232

Depreciation expense was $56 million, $55 million and $38 million for fiscal 2018, 2017 and 2016, respectively. During the quarter ended March 30, 2018, the Company determined that the carrying amount of a real estate property may not be recoverable and as a result recorded an impairment charge of $7 million, which was recorded within Corporate. On July 23, 2018, the Company entered into a Contract of Sale to sell and lease back the property. The term of the lease is expected to end during fiscal 2020. See "Note 27—Subsequent Events" regarding the completion of the sale.

Note 13—Fair Value Measurements

The Company's financial instruments measured on a recurring basis at fair value consisted of the following:

	December 28, 2018		December 29, 2017	
	Carrying value	Fair value	Carrying value	Fair value
	(in millions)			
Financial assets:				
Derivatives	$ —	$ —	$ 37	$ 37
Financial liabilities:				
Derivatives	35	35	—	—

The Company's derivatives consisted of the fair value interest rate swaps on its $450 million fixed rate 4.45% senior secured notes maturing in December 2020, and cash flow interest rate swaps on $1.5 billion of the Company's variable rate senior secured term loans (see "Note 14—Derivative Instruments"). The fair value of the fair value interest rate swaps and cash flow interest rate swaps is determined based on observed values for underlying interest rates on the LIBOR yield curve and the underlying interest rate, respectively (Level 2 inputs).

The Company's financial instruments measured on a recurring basis at fair value also includes its defined benefit plan assets (Level 2 inputs). See "Note 21—Retirement Plans" for further details on these investments.

The carrying amounts of the Company's financial instruments, other than derivatives, which include cash equivalents, accounts receivable, other short-term receivable, accounts payable and accrued expenses, are reasonable estimates of their related fair values. The carrying value of the Company's notes receivable (see "Note 7—Divestitures" and "Note 22—Leases") of $24 million and $63 million as of December 28, 2018, and December 29, 2017, respectively, approximates fair value as the stated interest rates within the agreements are consistent with the current market rates used in notes with similar terms in the market (Level 2 inputs).

As of December 28, 2018, and December 29, 2017, the fair value of debt was $3.1 billion and $3.2 billion, respectively, and the carrying amount was $3.1 billion for both periods (see "Note 15—Debt"). The fair value of long-term debt is determined based on current interest rates available for debt with terms and maturities similar to the Company's existing debt arrangements (Level 2 inputs).

During fiscal 2018 and 2017, the Company did not have any assets or liabilities measured at fair value on a non-recurring basis, other than a real estate property measured at fair value (Level 2) on March 30, 2018, which resulted in an impairment charge of $7 million (see "Note 12—Property, Plant and Equipment").

Note 14—Derivative Instruments

The fair value of the Company's interest rate swaps was as follows:

	Asset derivatives		
	Balance sheet line item	December 28, 2018	December 29, 2017
		(in millions)	
Cash flow interest rate swaps	Other assets	$ —	$ 37

	Liability derivatives		
	Balance sheet line item	December 28, 2018	December 29, 2017
		(in millions)	
Fair value interest rate swaps	Other long-term liabilities	$ 3	$ —
Cash flow interest rate swaps			