UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2023

☐ **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 001-41565

Leonardo DRS, Inc.
(Exact Name of Registrant as Specified in its Charter)

Delaware	**13-2632319**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification Number)**

2345 Crystal Drive
Suite 1000
Arlington, Virginia 22202
(703) 416-8000
(Address, including zip code, and telephone number, including area code, of registrant’s principal executive offices)

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

Title of each class	Trading Symbol	Name of each exchange on which registered
Common stock, $0.01 par value	DRS	Nasdaq Stock Market LLC

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

Indicate by check mark whether the registrant has submitted electronically 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 ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and an emerging growth company in Rule 12b-2 of the Exchange Act.

Large accelerated filer	☐	Accelerated filer	☐
Non-accelerated filer	☒	Smaller reporting company	☐
		Emerging growth company	☐

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 7(a)(2)(B) of the Securities Act. ☐

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

As of November 1, 2023, there were 262,370,008 shares of the registrant’s common stock, par value of $0.01 per share, outstanding.

TABLE OF CONTENTS

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS AND INFORMATION

In this quarterly report on Form 10-Q (the “Quarterly Report”), when using the terms the “Company,” “DRS,” “we,” “us” and “our,” unless otherwise indicated or the context otherwise requires, we are referring to Leonardo DRS, Inc. This Quarterly Report contains forward-looking statements and cautionary statements within the meaning of the Private Securities Litigation Reform Act of 1995. Some of the forward-looking statements can be identified by the use of forward-looking terms such as “believes,” “expects,” “may,” “will,” “shall,” “should,” “would,” “could,” “seeks,” “aims,” “strives,” “targets,” “projects,” “intends,” “plans,” “estimates,” “anticipates” or other comparable terms. Forward-looking statements include, without limitation, all matters that are not historical facts. They appear in a number of places throughout this Quarterly Report and include, without limitation, statements regarding our intentions, beliefs, assumptions or current expectations concerning, among other things, financial goals, financial position, results of operations, cash flows, prospects, strategies or expectations, and the impact of prevailing economic conditions.

Forward-looking statements are subject to known and unknown risks and uncertainties, many of which may be beyond our control. We caution you that forward-looking statements are not guarantees of future performance or outcomes and that actual performance and outcomes may differ materially from those made in or suggested by the forward-looking statements contained in this Quarterly Report. In addition, even if future performance and outcomes are consistent with the forward-looking statements contained in this Quarterly Report, those results or developments may not be indicative of results or developments in subsequent periods. New factors emerge from time to time that may cause our business not to develop as we expect, and it is not possible for us to predict all of them. Factors that could cause actual results and outcomes to differ from those reflected in forward-looking statements include, without limitation:

- Disruptions or deteriorations in our relationship with the relevant agencies of the U.S. government, as well as any failure to pass routine audits or otherwise comply with governmental requirements including those related to security clearance or procurement rules, including the False Claims Act;
- Significant delays or reductions in appropriations for our programs and changes in U.S. government priorities and spending levels more broadly;
- Any failure to comply with the proxy agreement with the U.S. Department of Defense (the “DoD”);
- Our relationships with other industry participants, including any contractual disputes or the inability of our key suppliers to timely deliver our components, parts or services;
- Failure to properly contain a global pandemic in a timely manner could materially affect how we and our business partners operate;
- The effect of inflation on our supply chain and/or our labor costs;
- Our mix of fixed-price, cost-plus and time-and-material type contracts and any resulting impact on our cash flows due to cost overruns;
- Failure to properly comply with various covenants of the agreements governing our debt could negatively impact our business;
- Our dependence on U.S. government contracts, which often are only partially funded and are subject to immediate termination, some of which are classified, and the concentration of our customer base in the U.S. defense industry;
- Our use of estimates in pricing and accounting for many of our programs that are inherently uncertain and which may not prove to be accurate;
- Our ability to realize the full value of our backlog;

- Our ability to predict future capital needs or to obtain additional financing if we need it;
- Our ability to respond to the rapid technological changes in the markets in which we compete;
- The effect of global and regional economic downturns and rising interest rates;
- Our ability to meet the requirements of being a public company;
- Our ability to maintain an effective system of internal control over financial reporting;
- Our inability to appropriately manage our inventory;
- Our inability to fully realize the value of our total estimated contract value or bookings;
- Our ability to compete efficiently, including due to U.S. government organizational conflict of interest rules which may limit new contract opportunities or require us to wind down existing contracts;
- Preferences for set-asides for minority-owned, small and small disadvantaged businesses could impact our ability to be a prime contractor;
- Any failure to meet our contractual obligations including due to potential impacts to our business from supply chain risks, such as longer lead times and shortages of electronics and other components;
- Any security breach, including any cyber-attack, cyber intrusion, insider threat, or other significant disruption of our IT networks and related systems, or those of our customers, suppliers, vendors, subcontractors, partners, or other third parties, as well as any act of terrorism or other threat to our physical security and personnel;
- Our ability to fully exploit or obtain patents or other intellectual property protections necessary to secure our proprietary technology, including our ability to avoid infringing upon the intellectual property of third parties or prevent third parties from infringing upon our own intellectual property;
- The conduct of our employees, agents, affiliates, subcontractors, suppliers, business partners or joint ventures in which we participate which may impact our reputation and ability to do business;
- Our compliance with environmental laws and regulations, and any environmental liabilities that may affect our reputation or financial position;
- The outcome of litigation, arbitration, investigations, claims, disputes, enforcement actions and other legal proceedings in which we are involved;
- Various geopolitical and economic factors, laws and regulations including the Foreign Corrupt Practices Act, the Export Control Act, the International Traffic in Arms Regulations, the Export Administration Regulations, and those that we are exposed to as a result of our international business, including their impact on our ability to access certain raw materials;
- Geopolitical conflicts, including the war in Israel, have the potential to evolve quickly, creating uncertainty in the world and broader Middle East region specifically, along with the potential for disruptions to our Israeli operations, including but not limited to workforce calls for duty, transportation and other logistical impacts and reduced customer confidence;
- Our ability to obtain export licenses necessary to conduct certain operations abroad, including any attempts by Congress to prevent proposed sales to certain foreign governments;
- Our ability to attract and retain technical and other key personnel;
- The occurrence of prolonged work stoppages;

- The unavailability or inadequacy of our insurance coverage, customer indemnifications or other liability protections to cover all of our significant risks or to pay for material losses we incur;
- Future changes in U.S. tax laws and regulations or interpretations thereof;
- Certain limitations on our ability to use our net operating losses to offset future taxable income;
- Termination of our leases or our inability to renew our leases on acceptable terms;
- Changes in estimates used in accounting for our pension plans, including in respect of the funding status thereof;
- Changes in future business or other market conditions that could cause business investments and/or recorded goodwill or other long-term assets to become impaired;
- Adverse consequences from any acquisitions such as operating difficulties, dilution and other harmful consequences or any modification, delay or prevention of any future acquisition or investment activity by the Committee on Foreign Investment in the United States;
- Natural disasters or other significant disruptions; or
- Any conflict of interest that may arise because Leonardo US Holding, LLC ("US Holding"), our majority stockholder, or Leonardo S.p.A., our ultimate majority stockholder, may have interests that are different from, or conflict with, those of our other stockholders, including as a result of any ongoing business relationships Leonardo S.p.A. may have with us, and their significant ownership in us may discourage change of control transactions (our amended and restated certificate of incorporation provides that we waive any interest or expectancy in corporate opportunities presented to Leonardo S.p.A); or
- Our obligations to provide certain services to Leonardo S.p.A., which may divert human and financial resources from our business.

You should read this Quarterly Report completely and with the understanding that actual future results may be materially different from expectations. All forward-looking statements made in this Quarterly Report are qualified by these cautionary statements. These forward-looking statements are made only as of the date of this filing, and we do not undertake any obligation, other than as may be required by law, to update or revise any forward-looking or cautionary statements to reflect changes in assumptions, the occurrence of events, unanticipated or otherwise, and changes in future operating results over time or otherwise.

Other risks, uncertainties and factors, including those discussed under "Risk Factors" in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2022, filed with the SEC on March 28, 2023 and those discussed under "Risk Factors" in Part II, Item 1A of this Quarterly Report, could cause our actual results to differ materially from those projected in any forward-looking statements we make. Readers should carefully read the discussion of these factors to better understand the risks and uncertainties inherent in our business and underlying any forward-looking statements.

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS (UNAUDITED)

LEONARDO DRS, INC.

Consolidated Statements of Earnings (Unaudited)

(Dollars in millions, except per share amounts)	Three Months Ended September 30, 2023	Three Months Ended September 30, 2022	Nine Months Ended September 30, 2023	Nine Months Ended September 30, 2022
Revenues:				
Products	$ 651	$ 580	$ 1,761	$ 1,670
Services	52	54	139	203
Total revenues	703	634	1,900	1,873
Cost of revenues:				
Products	(504)	(461)	(1,365)	(1,328)
Services	(37)	(43)	(97)	(154)
Total cost of revenues	(541)	(504)	(1,462)	(1,482)
Gross profit	162	130	438	391
General and administrative expenses	(96)	(101)	(286)	(261)
Amortization of intangibles	(5)	(3)	(16)	(7)
Other operating (expenses) income, net	(2)	350	(10)	351
Operating earnings	59	376	126	474
Interest expense	(10)	(9)	(27)	(27)
Other, net	(1)	—	(2)	—
Earnings before taxes	48	367	97	447
Income tax provision	1	88	3	107
Net earnings	$ 47	$ 279	$ 94	$ 340
Net earnings per share from common stock:				
Basic earnings per share	$ 0.18	$ 1.33	$ 0.36	$ 1.62
Diluted earnings per share	$ 0.18	$ 1.33	$ 0.36	$ 1.62

See accompanying Notes to Consolidated Financial Statements.

LEONARDO DRS, INC.

Consolidated Statements of Comprehensive Income (Unaudited)

(Dollars in millions)	Three Months Ended September 30, 2023	Three Months Ended September 30, 2022	Nine Months Ended September 30, 2023	Nine Months Ended September 30, 2022
Net earnings	$ 47	$ 279	$ 94	$ 340
Other comprehensive income (loss):				
Foreign currency translation loss, net of income taxes	(1)	(3)	—	(3)
Gain from pension settlements	—	—	—	3
Net unrecognized gain on postretirement obligations, net of income taxes	1	—	2	1
Other comprehensive income (loss), net of income tax	—	(3)	2	1
Total comprehensive income	$ 47	$ 276	$ 96	$ 341

See accompanying Notes to Consolidated Financial Statements.

LEONARDO DRS, INC.

Consolidated Balance Sheets

(Dollars in millions, except per share amounts)	(Unaudited) September 30, 2023	December 31, 2022
ASSETS		
Current assets:		
Cash and cash equivalents	$ 47	$ 306
Accounts receivable, net	200	166
Contract assets	1,061	872
Inventories	383	319
Prepaid expenses	17	20
Other current assets	32	24
Total current assets	1,740	1,707
Noncurrent assets:		
Property, plant and equipment, net	399	404
Intangible assets, net	156	172
Goodwill	1,236	1,236
Deferred tax assets	87	66
Other noncurrent assets	95	92
Total noncurrent assets	1,973	1,970
Total assets	$ 3,713	$ 3,677
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Short-term borrowings and current portion of long-term debt	$ 132	$ 29
Accounts payable	328	457
Contract liabilities	258	233
Other current liabilities	233	323
Total current liabilities	951	1,042
Noncurrent liabilities:		
Long-term debt	351	365
Pension and other postretirement benefit plan liabilities	35	45
Deferred tax liabilities	8	—
Other noncurrent liabilities	126	98
Total noncurrent liabilities	520	508
Commitments and contingencies (Note 14)		
Shareholders' equity:		
Preferred stock, $0.01 par value: 10,000,000 shares authorized; none issued	—	—
Common stock, $0.01 par value: 350,000,000 shares authorized; 262,039,337 and 260,234,033 issued as of September 30, 2023 and December 31, 2022, respectively	3	3
Additional paid-in capital	5,166	5,147
Accumulated deficit	(2,880)	(2,974)
Accumulated other comprehensive loss	(47)	(49)
Total shareholders' equity	2,242	2,127
Total liabilities and shareholders' equity	$ 3,713	$ 3,677

See accompanying Notes to Consolidated Financial Statements.

LEONARDO DRS, INC.

Consolidated Statements of Cash Flows (Unaudited)

(Dollars in millions)	Nine Months Ended September 30, 2023	Nine Months Ended September 30, 2022
Operating activities		
Net earnings	$ 94	$ 340
Adjustments to reconcile net earnings to net cash used in operating activities:		
Depreciation and amortization	63	48
Deferred income taxes	(13)	10
Gain from sale of business	—	(350)
Other	13	—
Changes in assets and liabilities:		
Accounts receivable	(34)	(17)
Contract assets	(189)	(174)
Inventories	(64)	(43)
Prepaid expenses	3	—
Other current assets	(8)	(2)
Other noncurrent assets	13	10
Defined benefit obligations	(8)	(4)
Other current liabilities	(82)	83
Other noncurrent liabilities	6	(3)
Accounts payable	(129)	(180)
Contract liabilities	25	36
Net cash used in operating activities	(310)	(246)
Investing activities		
Capital expenditures	(42)	(35)
Proceeds from sales of businesses	—	483
Net cash (used in) provided by investing activities	(42)	448
Financing activities		
Net decrease in third party borrowings (maturities of 90 days or less)	(11)	(12)
Repayment of third party debt	(454)	—
Borrowings of third party debt	555	—
Repayment of related party debt	—	(640)
Borrowings from related parties	—	675
Dividend to US Holding	—	(396)
Proceeds from stock issuance	8	—
Cash outlay to reacquire equity instruments	(1)	—
Other	(4)	(6)
Net cash provided by (used in) financing activities	93	(379)
Effect of exchange rate changes on cash and cash equivalents	—	—
Net decrease in cash and cash equivalents	(259)	(177)
Cash and cash equivalents at beginning of year	306	240
Cash and cash equivalents at end of period	$ 47	$ 63

See accompanying Notes to Consolidated Financial Statements.

LEONARDO DRS, INC.

Consolidated Statements of Shareholders' Equity (Unaudited)

(Dollars in millions)	Common stock	Additional paid- in capital	Accumulated other comprehensive loss	Accumulated deficit	Total
Balance as of December 31, 2021	$ 1	$ 4,633	$ (58)	$ (2,983)	$ 1,593
Total comprehensive income	—	—	1	340	341
Dividend to US Holding	—	—	—	(396)	(396)
Balance as of September 30, 2022	$ 1	$ 4,633	$ (57)	$ (3,039)	$ 1,538
Balance as of December 31, 2022	$ 3	$ 5,147	$ (49)	$ (2,974)	$ 2,127
Total comprehensive income	—	—	2	94	96
Stock compensation expense	—	19	—	—	19
Balance as of September 30, 2023	$ 3	$ 5,166	$ (47)	$ (2,880)	$ 2,242

See accompanying Notes to Consolidated Financial Statements.

LEONARDO DRS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies

A. Organization

Leonardo DRS, Inc., together with its wholly owned subsidiaries (hereinafter, “DRS,” “the Company,” “us,” “our,” or “we”) is a supplier of defense electronics products, systems and military support services. The Company’s largest shareholder is Leonardo S.p.A (hereinafter, “Leonardo S.p.A.”), an Italian multi-national aerospace, defense and security company headquartered in Rome, Italy, through its ultimate sole ownership of Leonardo US Holding, LLC (“US Holding”). US Holding is the majority stockholder of the Company.

DRS is a provider of defense products and technologies that are used across land, air, sea, space and cyber domains. Our diverse array of defense systems and solutions are offered to all branches of the U.S. military, major aerospace and defense prime contractors, government intelligence agencies, international military customers and industrial markets for deployment on a wide range of military platforms. We focus our capabilities in areas of critical importance to the U.S. military, such as advanced sensing, network computing, force protection and electrical power and propulsion.

These capabilities directly align with our two reportable segments: Advanced Sensing and Computing and Integrated Mission Systems. The U.S. DoD is our largest customer and accounts for approximately 80% and 82% of our total revenues as an end-user for the nine months ended September 30, 2023 and September 30, 2022, respectively. Specific international and commercial market opportunities exist within these segments and make up approximately 20% and 18% of our total revenues for the nine months ended September 30, 2023 and September 30, 2022, respectively. Our two reportable segments reflect the way performance is assessed and resources are allocated by our Chief Executive Officer, who is our chief operating decision maker (“CODM”).

Advanced Sensing and Computing

The Advanced Sensing and Computing (“ASC”) segment designs, develops and manufactures sensing and network computing technology that enables real-time situational awareness required for enhanced operational decision making and execution by our customers.

Our leading sensing capabilities span applications including missions requiring advanced detection, precision targeting and surveillance sensing, long range electro-optic/infrared (“EO/IR”), signals intelligence (“SIGINT”) and other intelligence systems, electronic warfare (“EW”), ground vehicle sensing, next generation active electronically scanned array (“AESA”) tactical radars, dismounted soldier sensing and space sensing. Across our offering, we are focused on advancing sensor distance, precision, clarity, definition, spectral depth and effectiveness. Furthermore, we seek to leverage our multi-decade experience to optimize size, weight, power and cost tailored to our customers’ specific mission requirements, including in space-based applications for earth surveillance and missile tracking.

Our sensing capabilities are complemented by our rugged, trusted and cyber resilient network computing products. Our network computing offering is utilized across a broad range of mission applications including platform computing on ground and shipboard (both surface ship and submarine) for advanced battle management, combat systems, radar, command and control (“C2”), tactical networks, tactical computing and communications. Our network computing products support the DoD’s need for greater situational understanding at the tactical edge and permits data to be rapidly transmitted securely from command centers to forward-positioned defense assets.

Integrated Mission Systems

Our Integrated Mission Systems (“IMS”) segment designs, develops, manufactures and integrates power conversion, control and distribution systems, ship propulsion systems, motors and variable frequency drives, force protection systems, transportation and logistics systems for the U.S. and allied defense customers.

Our naval power and propulsion systems are providing next-generation power capabilities for the future fleet. DRS is currently a leading provider of next-generation electrical propulsion systems for the U.S. Navy. We provide power conversion, control, distribution and propulsion systems for the Navy's top priority shipbuilding programs, including the Columbia Class ballistic missile submarine, the first modern U.S. electric drive submarine. We believe DRS is well positioned to meet the needs of an increasingly electrified fleet with our high-efficiency, power dense permanent magnet motors, energy storage systems and associated efficient, rugged and compact power conversion, electrical actuation systems, and advanced cooling technologies. DRS has a long history of providing a number of other critical products to the U.S. Navy with a significant installed base on submarines, aircraft carriers and other surface ships including motor controllers, instrumentation and control equipment, electrical actuation systems, and thermal management systems for electronics and ship stores refrigeration.

Our technologies and systems help protect U.S. forces and assets against increasingly sophisticated and proliferating threats. DRS is an integrator of systems in ground vehicles for short-range air defense, counter-Unmanned Aerial Systems ("C-UAS"), and vehicle survivability and protection. This integrator role includes utilizing radars, EW equipment, reconnaissance and surveillance systems, modular combat vehicle turrets, and stabilized sensor suites, and kinetic countermeasures for short-range air defense. Our force protection systems, including solutions for C-UAS, short-range air defense systems and active protection systems used to defend ground combat vehicles help protect personnel and defense assets from these growing threats.

Other

The Company separately presents the unallocable costs associated with corporate functions and certain non-operating subsidiaries of the Company as Corporate & Eliminations.

See *Note 16*: *Segment Information* for further information regarding our business segments.

B. Basis of presentation

The accompanying unaudited Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") and include the accounts of DRS, its wholly owned subsidiaries and its controlling interests and contain all adjustments, which are of a normal and recurring nature, considered necessary by management to present fairly the financial position, results of operations and cash flows for the periods presented. Interests in ventures that are controlled by the Company, or for which the Company is otherwise deemed to be the primary beneficiary, are consolidated. For joint ventures in which the Company does not have a controlling interest, but exerts significant influence, the Company applies the equity method of accounting. All intercompany transactions and balances have been eliminated in consolidation. Certain prior year amounts have been reclassified to conform to current year presentation.

Interim Financial Statements. The unaudited Consolidated Financial Statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). These rules and regulations permit some of the information and footnote disclosures included in financial statements prepared in accordance with U.S. GAAP to be condensed or omitted.

These unaudited Consolidated Financial Statements should be read in conjunction with our audited Consolidated Financial Statements as of and for the year ended December 31, 2022 included in our Annual Report on Form 10-K for the year ended December 31, 2022, filed with the SEC on March 28, 2023.

C. New Accounting Pronouncements

Disclosure of Supplier Finance Program Obligations

In September 2022, the Financial Accounting Standards Board issued Accounting Standards Update 2022-04, *Liabilities – Supplier Finance Programs (Subtopic 405-50): Disclosure of Supplier Finance Program Obligations*, which is effective for fiscal years beginning after December 15, 2022, including interim periods within those fiscal years. The adoption of this standard did not have a material impact on our financial statements.

Note 2. Business Acquisitions and Dispositions

Acquisitions

On June 21, 2022, the Company, entered into an Agreement and Plan of Merger (the "Merger Agreement") with RADA Electronic Industries, Ltd ("RADA"), a leading Israel-based provider of small-form tactical radar, for an all-stock merger, with RADA surviving as a wholly owned subsidiary of the Company. The Company acquired RADA as part of the Company's goal to become a market leader in advanced sensing and force protection.

The acquisition of RADA has been accounted for using the acquisition method of accounting in accordance with ASC 805, *Business Combinations,* with the Company as the accounting acquirer, which requires the assets acquired and liabilities assumed be recognized at their acquisition date fair value. The acquisition was completed on November 28, 2022, when each issued and outstanding ordinary share of RADA was converted and exchanged for one share of common stock of the Company.

The total purchase consideration for RADA was $511 million and is comprised of the Company's shares of common stock issued in exchange for all issued and outstanding ordinary shares of RADA, as well as $20 million of replacement stock compensation awards' fair value attributable to pre-combination services.

The preliminary fair value estimates of the net assets acquired and liabilities assumed are based upon preliminary calculations and valuations, and those estimates and assumptions are subject to change as the Company obtains additional information during the measurement period (up to one year from the acquisition date). The Company has not yet finalized the determination of fair values allocated to the acquired assets and liabilities, including but not limited to the valuation of contract related assets and liabilities and related tax impacts of the opening balance sheet adjustments. The excess of the total consideration over the tangible assets, identifiable intangible assets, and assumed liabilities is recorded as goodwill. Identifiable intangibles assets of $131 million consist of $90 million of technology related assets while the remaining $41 million consists of customer and contractual relationships. The goodwill of $284 million arising from the acquisition is primarily attributable to the growth opportunities related to the RADA business. None of the goodwill resulting from the acquisition is deductible for tax purposes. All of the goodwill recognized related to the RADA acquisition was assigned to the ASC segment.

Dispositions

On March 21, 2022, the Company entered into a definitive agreement to sell its Global Enterprise Solutions ("GES") business to SES Government Solutions, Inc., a wholly-owned subsidiary of SES S.A., for $450 million subject to certain working capital adjustments. The transaction was completed on August 1, 2022 and resulted in cash proceeds of $427 million after net working capital adjustments.

In February 2022, the Company's Board of Directors approved the strategic initiative to divest the Company's interest in Advanced Acoustic Concepts ("AAC"). On April 19, 2022, we entered into a definitive sales agreement to divest our share of our equity investment in AAC for $56 million to Thales Defense & Security, Inc., the minority partner in AAC. The transaction was completed on July 8, 2022 and resulted in proceeds of $56 million.

Note 3. Revenue from Contracts with Customers

The Company recognizes revenue for each separately identifiable performance obligation in a contract representing an obligation to transfer a distinct good or service to a customer. In most cases, goods and services provided under the Company's contracts are accounted for as single performance obligations due to the complex and integrated nature of our products and services. These contracts generally require significant integration of a group of goods and/or services to deliver a combined output. In some contracts, the Company provides multiple distinct goods or services to a customer. In those cases, the Company accounts for the distinct contract deliverables as separate performance obligations and allocates the transaction price to each performance obligation based on its relative standalone selling price, which is generally estimated using cost plus a reasonable margin. We classify revenues as products or services on our Consolidated Statements of Earnings based on the predominant attributes of the performance obligations. While the Company provides warranties on certain contracts, we typically do not provide for services beyond standard assurances and therefore do not consider warranties to be separate performance obligations. Typically we enter into three types of contracts: fixed-price contracts, cost-plus contracts and time and material (“T&M”) contracts (cost-plus contracts and T&M contracts are aggregated below as flexibly priced contracts). The majority of our total revenues are derived from fixed-price contracts; refer to the revenue disaggregation disclosures that follow.

For fixed-price contracts, customers agree to pay a fixed amount, negotiated in advanced for a specified scope of work.

For cost-plus contracts, typically we are reimbursed for allowable or otherwise defined total costs (defined as cost of revenues plus allowable general and administrative expenses) incurred, plus a fee. The contracts may also include incentives for various performance criteria, including quality, timeliness and cost-effectiveness. In addition, costs are generally subject to review by clients and regulatory audit agencies, and such reviews could result in costs being disputed as non-reimbursable under the terms of the contract.

T&M contracts provide for reimbursement of labor hours expended at a contractual fixed labor rate per hour, plus the actual costs of material and other direct non-labor costs. The fixed labor rates on T&M contracts include amounts for the cost of direct labor, indirect contract costs and profit.

Revenue from contracts with customers is recognized when the performance obligations are satisfied through the transfer of control over the good or service to the customer, which may occur either over time or at a point in time.

Revenues for the majority of our contracts are measured using the over time, percentage of completion cost-to-cost method of accounting to calculate percentage of completion. We believe this is an appropriate measure of progress toward satisfaction of performance obligations as this measure most accurately depicts the progress of our work and transfer of control to our customers. Due to the long-term nature of many of our contracts, developing the estimated total cost at completion and total transaction price often requires judgment. Factors that must be considered in estimating the cost of the work to be completed include the nature and complexity of the work to be performed, subcontractor performance and the risk and impact of delayed performance.

After establishing the estimated total cost at completion, we follow a standard Estimate at Completion (“EAC”) process in which we review the progress and performance on our ongoing contracts on a routine basis. Adjustments to original estimates for a contract's revenue, estimated costs at completion and estimated profit or loss often are required as work progresses under a contract, as experience is gained and as more information is obtained, even though the scope of work required under the contract may not change and are also required if contract modifications occur. When adjustments in estimated total costs at completion or in estimated total transaction price are determined, the related impact on revenue and operating income are recognized using the cumulative catch-up method, which recognizes in the current period the cumulative effect of such adjustments for all prior periods. Any anticipated losses on these contracts are fully recognized in the period in which the losses become evident.

EAC adjustments had the following impacts to revenue for the periods presented:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in millions)	2023	2022	2023	2022
Revenue	$ 6	$ (11)	$ (14)	$ (22)
Total % of Revenue	0.9 %	1.8 %	0.7 %	1.2 %

The impacts noted above are attributed primarily to changes in our firm-fixed-price development type programs. As changes happen in the design required to achieve contractual specifications, those changes often result in the programs’ estimate and related profitability.

Conversely, if the requirements for the recognition of contracts over time are not met, revenue is recognized at a point in time when control transfers to the customer, which is generally upon transfer of title. In such cases, the production that is in progress and costs that will be recognized at a future point in time are reported within “inventories.”

Costs to obtain a contract are incremental direct costs incurred to obtain a contract with a customer, including sales commissions and dealer fees, and are capitalized if material. Costs to fulfill a contract include costs directly related to a contract or specific anticipated contract (e.g., certain design costs) that generate or enhance our ability to satisfy our performance obligations under these contracts. These costs are capitalized to the extent they are expected to be recovered from the associated contract.

Contract Assets and Liabilities

The timing of revenue recognition, billings and cash collections results in billed accounts receivable, unbilled receivables (contract assets), and customer advances and deposits (contract liabilities) on the Consolidated Balance Sheets. Amounts are billed as work progresses in accordance with agreed-upon contractual terms, either at periodic intervals (e.g., biweekly or monthly) or upon achievement of contractual milestones. Generally, billing occurs subsequent to revenue recognition, resulting in contract assets. However, we sometimes receive advances or deposits from our customers before revenue is recognized, resulting in contract liabilities. Contract assets and contract liabilities as of the dates presented were:

(Dollars in millions)	**September 30, 2023**	**December 31, 2022**
Contract assets	$ 1,061	$ 872
Contract liabilities	258	233
Net contract assets	$ 803	$ 639

Revenue recognized in the nine months ending September 30, 2023 and September 30, 2022, that was included in the contract liability balance at the beginning of each period was $157 million and $121 million, respectively.

Contract assets related to amounts withheld by customers until contract completion are not considered a significant financing component of our contracts because the intent is to protect the customers from our failure to satisfactorily complete our performance obligations. Payments received from customers in advance of revenue recognition (contract liabilities) are not considered a significant financing component of our contracts because they are utilized to pay for contract costs within a one-year period or are requested by us to ensure the customers meet their payment obligations.

Value of Remaining Performance Obligations

The value of remaining performance obligations, which we also refer to as total backlog, includes the following components:

- Funded - Funded backlog represents the revenue value of orders for services under existing contracts for which funding is appropriated or otherwise authorized less revenue previously recognized on these contracts.
- Unfunded - Unfunded backlog represents the revenue value of firm orders for products and services under existing contracts for which funding has not yet been appropriated less funding previously recognized on these contracts.

The following table summarizes the value of our total backlog as of September 30, 2023, incorporating both funded and unfunded components:

(Dollars in millions)	**September 30, 2023**
Funded	$ 3,356
Unfunded	1,363
Total Backlog	$ 4,719

We expect to recognize approximately 17% of our September 30, 2023 backlog as revenue over the next three months, with the remainder to be recognized thereafter. Subsequent to the third quarter, the Company agreed to contract terms and pricing totaling over $3 billion, for the majority of our electric power and propulsion system on the remaining seven Columbia Class submarines. The award is not included in the backlog numbers noted above.

Disaggregation of Revenue

ASC: ASC revenue is primarily derived from U.S. government development and production contracts and is generally recognized using the over time, percentage of completion cost-to-cost method of accounting. We disaggregate ASC revenue by geographical region, customer relationship and contract type. We believe these categories best depict how the nature, amount, timing and uncertainty of ASC revenue and cash flows are affected by economic factors:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in millions)	2023	2022	2023	2022
Revenue by Geographical Region				
United States	$ 376	$ 364	$ 1,046	$ 1,103
International	50	41	162	137
Intersegment Sales	5	3	18	8
Total	$ 431	$ 408	$ 1,226	$ 1,248
Revenue by Customer Relationship				
Prime contractor	$ 227	$ 216	$ 570	$ 664
Subcontractor	199	189	638	576
Intersegment Sales	5	3	18	8
Total	$ 431	$ 408	$ 1,226	$ 1,248
Revenue by Contract Type				
Firm Fixed Price	$ 356	$ 349	$ 1,015	$ 1,085
Flexibly Priced[(1)]	70	56	193	155
Intersegment Sales	5	3	18	8
Total	$ 431	$ 408	$ 1,226	$ 1,248

(1) Includes revenue derived from time-and-materials contracts.

IMS: IMS revenue is primarily derived from U.S. government development and production contracts and is generally recognized over time using the over time, percentage of completion cost-to-cost method of accounting. We disaggregate IMS revenue by geographical region, customer relationship and contract type. We believe these categories best depict how the nature, amount, timing and uncertainty of IMS revenue and cash flows are affected by economic factors:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in millions)	2023	2022	2023	2022
Revenue by Geographical Region				
United States	$ 272	$ 222	$ 680	$ 612
International	5	7	12	21
Intersegment Sales	—	—	—	1
Total	$ 277	$ 229	$ 692	$ 634
Revenue by Customer Relationship				
Prime contractor	$ 62	$ 41	$ 156	$ 110
Subcontractor	215	188	536	523
Intersegment Sales	—	—	—	1
Total	$ 277	$ 229	$ 692	$ 634
Revenue by Contract Type				
Firm Fixed Price	$ 234	$ 195	$ 572	$ 542
Flexibly Priced[1]	43	34	120	91
Intersegment Sales	—	—	—	1
Total	$ 277	$ 229	$ 692	$ 634

(1) Includes revenue derived from time-and-materials contracts.

Note 4. Accounts Receivable

Accounts receivable represent amounts billed and currently due from customers. Payment is typically received from our customers either at periodic intervals (e.g., biweekly, or monthly) or upon achievement of contractual milestones.

Accounts receivable consist of the following:

(Dollars in millions)	September 30, 2023	December 31, 2022
Accounts receivable	$ 201	$ 168
Less allowance for credit losses	(1)	(2)
Accounts receivable, net	$ 200	$ 166

The Company maintains certain agreements with financial institutions to sell certain trade receivables. See *Note 5: Sale of Receivables* for more information.

Note 5. Sale of Receivables

The Company is party to factoring facilities with various financial institutions with an aggregate capacity of $275 million. Pursuant to the servicing agreements, collections on sold receivables that had not yet been remitted to the financial institutions are included within short-term borrowings and current portion of long-term debt in the Consolidated Balance Sheets. See *Note 11: Debt* for further information.

The receivables sold under the factoring facilities are without recourse for any customer credit risk and result in a true sale. Receivables are derecognized in their entirety when sold, and the Company's continuing involvement is limited to their servicing, for which the Company receives a fee commensurate with the service provided and therefore no servicing asset or liability related to these receivables was recognized for any period presented. The fair value of the sold receivables approximated their book value due to their short-term nature. Proceeds from the sold receivables are reflected in operating cash flows on the Consolidated Statements of Cash Flows.

During the periods ended September 30, 2023 and September 30, 2022, the Company incurred immaterial purchase discount fees which are presented in other general and administrative expenditures, net on the Consolidated Statements of Earnings.

The table below summarizes the activity under the factoring facilities:

	Nine Months Ended September 30,	
(Dollars in millions)	2023	2022
Beginning balance	$ 243	$ 215
Sales of receivables	110	137
Cash returned to purchaser	(332)	(317)
Outstanding balance sold to purchasers[(1)]	21	35
Cash collected, not remitted to purchaser[(2)]	(1)	(3)
Remaining sold receivables	$ 20	$ 32

(1) For the nine months ended September 30, 2023 and September 30, 2022, the Company recorded a net decrease to cash flows from operating activities of $222 million and $180 million, respectively, from sold receivables.

(2) Represents cash collected on behalf of purchasers and not yet remitted.

Note 6. Inventories

Inventories consists of the following:

(Dollars in millions)	September 30, 2023	December 31, 2022
Raw materials	$ 76	$ 83
Work in progress	293	224
Finished goods	14	12
Total	$ 383	$ 319

Note 7. Property, Plant and Equipment

Property, plant and equipment by major asset class consists of the following:

(Dollars in millions)	September 30, 2023	December 31, 2022
Land, buildings and improvements	$ 342	$ 321
Plant and machinery	201	190
Equipment and other	338	335
Total property, plant and equipment, at cost	881	846
Less accumulated depreciation	(482)	(442)
Total property, plant and equipment, net	$ 399	$ 404

Depreciation expense related to property, plant and equipment was $47 million and $41 million for the nine months ended September 30, 2023 and September 30, 2022, respectively.

Note 8. Other Liabilities

A summary of significant other liabilities by balance sheet caption follows:

(Dollars in millions)	September 30, 2023	December 31, 2022
Salaries, wages and accrued bonuses	$ 64	$ 63
Fringe benefits	63	76
Litigation	—	10
Restructuring costs	10	4
Provision for contract losses	41	54
Operating lease liabilities	23	25
Taxes payable	2	31
Other[1]	30	60
Total other current liabilities	$ 233	$ 323
Operating lease liabilities	$ 72	$ 68
Taxes payable	32	21
Other[1]	22	9
Total other noncurrent liabilities	$ 126	$ 98

(1) Consists primarily of environmental remediation reserves and warranty reserves. See *Note 14: Commitments and Contingencies* for more information regarding the warranty provision.

Note 9. Intangible Assets

Other intangible assets mainly refer to the fair value of existing customer contractual relationships attributable to the acquired business and patents which are being amortized over their respective lives. The fair value of intangible assets typically is determined, as of the date of acquisition, based on estimates and judgments regarding expectations for the estimated future after-tax earnings and cash flows (including cash flows for working capital) arising from backlog and follow-on sales to the customer over their estimated lives, including the probability of expected future contract renewals and sales, less a contributory assets charge, all of which is discounted to present value.

The following disclosure presents certain information regarding the Company's intangible assets as of September 30, 2023 and December 31, 2022. All intangible assets are being amortized over their estimated useful lives, as indicated below, with no estimated residual values.

	September 30, 2023			December 31, 2022		
(Dollars in millions)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Acquired Intangible Assets	$ 1,087	$ (935)	$ 152	$ 1,087	$ (918)	$ 169
Patents and licenses	10	(6)	4	9	(6)	3
Total intangible assets	$ 1,097	$ (941)	$ 156	$ 1,096	$ (924)	$ 172

Amortization expense related to intangible assets was $5 million and $16 million for the three and nine months ended September 30, 2023, respectively, and $3 million and $7 million for the three and nine months ended September 30, 2022, respectively.

Customer relationships are amortized on a straight-line basis over their estimated useful lives of 10 to 15 years. Patents and licenses are amortized on a straight-line basis over their estimated useful lives of 5 to 10 years.

Note 10. Income Taxes

Our effective tax rate for the three and nine months ended September 30, 2023 was 2.1% and 3.1%, respectively. For the three and nine months ended September 30, 2023 the effective tax rate was lower than the U.S. Federal statutory rate of 21%, primarily due to a favorable impact for increasing our Research and Development Credit on our recently filed 2022 U.S. tax return.

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at September 30, 2023 and December 31, 2022 is as follows:

(Dollars in millions)	September 30, 2023	December 31, 2022
Deferred tax assets	$ 221	$ 208
Less valuation allowance	19	17
Deferred tax assets	202	191
Deferred tax liabilities	123	125
Net deferred tax asset	$ 79	$ 66

Our deferred tax balance associated with our retirement benefit plans includes a deferred tax asset of $8 million and $8 million as September 30, 2023 and December 31, 2022 respectively, that are recorded in accumulated other comprehensive earnings to recognize the funded status of our retirement plans. See *Note 12: Pension and Other Postretirement Benefits* for additional details.

Note 11. Debt

The Company’s debt consists of the following:

(Dollars in millions)	September 30, 2023	December 31, 2022
Term loan A	$ 217	$ 225
Outstanding revolver	110	—
Finance lease and other	157	161
Short-term borrowings	1	10
Total debt principal	485	396
Less unamortized debt issuance costs and discounts	(2)	(2)
Total debt, net	483	394
Less short-term borrowings and current portion of long-term debt	(132)	(29)
Total long-term debt	$ 351	$ 365

Term Loans

In November 2022, the Company entered into a senior unsecured credit agreement with Bank of America in the amount of $500 million (the “2022 Credit Agreement”) with a maturity of November 29, 2027. The 2022 Credit Agreement provides for a term loan of $225 million bearing interest at a variable rate generally based on the Secured Overnight Financing Rate (“SOFR”), plus a spread ranging from 1.48% to 2.10% depending on the leverage ratio, as defined in the 2022 Credit Agreement, or an alternative variable rate based on the higher of the Bank of America prime rate, the federal funds rate, or a rate generally based on SOFR, in each case subject to additional basis point spread as defined in the 2022 Credit Agreement (“2022 Term Loan A”). Interest is payable quarterly in arrears. The outstanding balance of the 2022 Term Loan A at September 30, 2023 was $217 million. The fair value of Term Loan A at September 30, 2023 was approximately $217 million; however, the Company has the ability to prepay the outstanding principal balance without penalty.

Credit Facilities

The 2022 Credit Agreement provides for a revolving credit facility available for working capital needs of the Company (“the 2022 Revolving Credit Facility”). As of September 30, 2023 and December 31, 2022, the 2022 Revolving Credit Facility had a limit of $275 million. Loans under the 2022 Revolving Credit Facility bear interest at a variable rate generally based on the SOFR, plus a spread ranging from 1.48% to 2.10% depending on the leverage ratio, as defined in the 2022 Credit Agreement, or an alternative variable rate based on the higher of the Bank of America prime rate, the federal funds rate, or a rate generally based on SOFR, in each case subject to additional basis point spread as defined in the 2022 Credit Agreement. The Company also pays a commitment fee ranging between 0.20% and 0.35% depending on the Company’s leverage ratio applied to the unused balance of the 2022 Revolving Credit Facility. The outstanding balance as of September 30, 2023 was $110 million and there was no outstanding balance on the 2022 Revolving Credit Facility as of December 31, 2022. The weighted average interest rate on the 2022 Revolving Credit Facility as of September 30, 2023 was 6.29%.

The Company also maintains uncommitted working capital credit facilities with certain financial institutions in an aggregate of $110 million and $65 million at September 30, 2023 and December 31, 2022, respectively (the “Financial Institution Credit Facilities”).

The primary purpose of the Financial Institution Credit Facilities is to support standby letter of credit issuances on contracts with customers. The Financial Institution Credit Facilities also included a revolving facility with a maximum borrowing limit of $15 million, which bore interest at LIBOR plus 0.5%. The revolving facility was eliminated from the Financial Institution Credit Facilities as of March 31, 2023. As of December 31, 2022, there was no balance outstanding on the revolving facility of the Financial Institution Credit Facilities. The Company had letters of credit outstanding of approximately $42 million and $36 million as of September 30, 2023 and December 31, 2022, which reduces the available capacity of the Financial Institution Credit Facilities by an equal amount.

Short-term Borrowings

As of September 30, 2023 and December 31, 2022, the Company recognized $1 million and $10 million, respectively, collected on behalf of the buyers of our trade receivables pursuant to our factoring arrangements as short-term borrowings and current portion of long-term debt in the Consolidated Balance Sheets, which approximates its fair value. Refer to *Note 4: Accounts Receivable* and *Note 5: Sale of Receivables* for more information.

Note 12. Pension and Other Postretirement Benefits

Retirement Plan Summary Information

The Company maintains multiple pension plans, both contributory and non-contributory, covering employees at certain locations. Eligibility requirements for participation in the plans vary, and benefits generally are based on the participant's compensation and years of service, as defined in the respective plan. The Company's funding policy generally is to contribute in accordance with cost accounting standards that affect government contractors, subject to the U.S. Internal Revenue Code of 1986, as amended (the “Tax Code”) and regulations thereunder. For all periods presented, the Company made no discretionary pension contributions. Plan assets are invested primarily in equities, bonds (both corporate and U.S. government), U.S. government-sponsored entity instruments, cash and cash equivalents and real estate.

The Company also provides postretirement medical benefits for certain retired employees and dependents at certain locations. Participants are eligible for these benefits when they retire from active service and meet the eligibility requirements for the Company's postretirement benefit plans. The Company's contractual arrangements with the U.S. government provide for the recovery of contributions to a Voluntary Employees' Beneficiary Association trust and, for non-funded plans, recovery of claims on a pay-as-you-go basis, subject to the Tax Code and regulations thereunder, with the retiree generally paying a portion of the costs through contributions, deductibles and coinsurance provisions.

The Company also maintains certain non-contributory and unfunded supplemental retirement plans. Eligibility for participation in the supplemental retirement plans is limited, and benefits generally are based on the participant's compensation and/or years of service.

The following tables provide certain information regarding the Company's pension, postretirement and supplemental retirement plans for the periods presented:

	Defined Benefit Pension Plans		Postretirement Benefit Plan		Supplemental Retirement Plans	
(Dollars in millions)	Three Months Ended September 30, 2023	Three Months Ended September 30, 2022	Three Months Ended September 30, 2023	Three Months Ended September 30, 2022	Three Months Ended September 30, 2023	Three Months Ended September 30, 2022
Service cost	$ —	$ —	$ —	$ —	$ —	$ —
Interest cost	2	1	—	—	1	—
Less expected return on plan assets	(2)	(1)	—	—	—	—
Amortization of net actuarial loss (gain)	—	—	—	—	—	—
Amortization of prior service cost	—	—	—	—	—	—
Settlement expense (income)	—	—	—	—	—	—
Net periodic benefit cost	$ —	$ —	$ —	$ —	$ 1	$ —

	Defined Benefit Pension Plans		Postretirement Benefit Plan		Supplemental Retirement Plans	
(Dollars in millions)	Nine Months Ended September 30, 2023	Nine Months Ended September 30, 2022	Nine Months Ended September 30, 2023	Nine Months Ended September 30, 2022	Nine Months Ended September 30, 2023	Nine Months Ended September 30, 2022
Service cost	$ —	$ —	$ —	$ —	$ —	$ —
Interest cost	6	4	—	—	1	1
Less expected return on plan assets	(5)	(5)	—	—	—	—
Amortization of net actuarial loss (gain)	1	1	—	—	—	—
Amortization of prior service cost	—	—	—	—	—	—
Settlement expense (income)	—	1	—	—	—	—
Net periodic benefit cost	$ 2	$ 1	$ —	$ —	$ 1	$ 1

The expected long-term return on plan assets assumption represents the average rate that the Company expects to earn over the long-term on the assets of the Company's benefit plans, including those from dividends, interest income and capital appreciation. The assumption has been determined based on expectations regarding future rates of return for the plans' investment portfolio, with consideration given to the allocation of investments by asset class and historical rates of return for each individual asset class.

Pension related expenses are reflected in the Total costs of revenues and General and administrative expenses on the Consolidated Statements of Earnings (unaudited).

A one percentage increase or decrease in healthcare trend rates in the table above would have an insignificant impact to our service and interest cost and the postretirement medical obligations.

Note 13. Earnings Per Share

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in millions, except per share amounts; shares in millions)	2023	2022	2023	2022
Net earnings	$ 47	$ 279	$ 94	$ 340
Basic weighted average number of shares outstanding	262	210	261	210
Impact of dilutive share-based awards	3	—	3	—
Diluted weighted average number of shares outstanding	265	210	264	210
Earnings per share attributable to common shareholders - basic	$ 0.18	$ 1.33	$ 0.36	$ 1.62
Earnings per share attributable to common shareholders - diluted	$ 0.18	$ 1.33	$ 0.36	$ 1.62

For the three and nine months ended September 30, 2023, potential dilutive common shares primarily consisted of employee stock options, restricted stock units (“RSUs”) and performance restricted stock units (“PRSUs”); however, the amount of dilutive securities included in the diluted weighted average number of shares outstanding was immaterial. For the three and nine months ended September 30, 2022, the basic and diluted weighted average number of shares outstanding were equal as there were no dilutive securities.

The computation of diluted earnings per share (“EPS”) excludes the effect of the potential exercise of stock awards when the average market price of the common stock is lower than the exercise price of the stock awards during the period because the effect would be anti-dilutive. In addition, the computation of diluted EPS excludes stock awards whose issuance is contingent upon the satisfaction of certain performance vesting conditions. At September 30, 2023, there were 2.0 million stock awards excluded from the computation. At September 30, 2022 there were no anti-dilutive securities.

Note 14. Commitments and Contingencies

Commitments

The Company’s commitments are primarily related to our lease agreements, purchase obligations, and credit agreements.

Contingencies

From time to time we are subject to certain legal proceedings and claims in the ordinary course of business. These matters are subject to many uncertainties and it is possible that some of these matters ultimately could be decided, resolved or settled in a manner adverse to us. Although the precise amount of liability that may result from these matters is not ascertainable, the Company believes that any amounts exceeding the Company's recorded accruals should not materially adversely affect the Company's financial condition or liquidity. It is possible, however, that the ultimate resolution of those matters could result in a material adverse effect on the Company's results of operations and/or cash flows from operating activities for a particular reporting period. We establish reserves for specific legal matters when we determine that the likelihood of an unfavorable outcome is probable and the loss is reasonably estimable. The Company reviews the developments in contingencies that could affect the amount of the reserves that have been previously recorded. The Company adjusts provisions and changes to disclosures accordingly to reflect the impact of negotiations, settlements, rulings, advice of legal counsel, and updated information. Significant judgment is required to determine both the probability and the estimated amount of any potential losses.

Some environmental laws, such as the Comprehensive Environmental Response, Compensation and Liability Act of 1980 (also known as “CERCLA” or the “Superfund law”) and similar state statutes, can impose liability upon former owners or operators for the entire cost of investigating and remediating contaminated sites regardless of the lawfulness of the original activities that led to the contamination. In July 2000, an entity which later became a subsidiary of the Company received a Section 104(e) Request for Information (“RFI”) from the National Park Service (“NPS”), pursuant to CERCLA, regarding the presence of radioactive material at a site within a national park (“Orphan Mine”), which site was operated by an alleged predecessor to our subsidiary over 50 years ago. Following the subsidiary’s response to the RFI, the NPS directed it and another alleged former operator to perform an Engineering Evaluation and Cost Analysis (“EE/CA”) of a portion of the site. The Company’s subsidiary made a good faith offer to conduct an alternative EE/CA work plan, but the NPS rejected this offer and opted to perform the EE/CA itself. The NPS previously posted its intention to open a formal public comment period regarding the EE/CA at the end of 2019. To the Company’s knowledge, the EE/CA has not been released and a public comment period has yet to be opened.

The Environmental Protection Agency (“EPA”) episodically updates its electronic databases concerning pending Superfund sites. As of June 2023, the entry in EPA’s Superfund database for this site states that this “[s]ite does not qualify for the NPL [National Priorities List] based on existing information. The EPA has determined that no further federal action (NFFA) will be taken at this site.” As a result, DRS has eliminated the Orphan Mine reserve as a liability is no longer probable or estimable. However, it remains possible that the NPS may seek to recover damages, including for remediation and/or loss of use of certain natural resources. The Company believes that it has legitimate defenses to its subsidiary’s potential liability and that there are other potentially responsible parties for the environmental conditions at the site, including the U.S. government as owner, operator and arranger at the site. The potential liability associated with this matter could change substantially due to such factors as additional information on the nature or extent of contamination, methods of remediation that might be recommended or required, changes in the apportionment of costs among the responsible parties, whether the NPS seeks to recover additional damages, whether the NPS’s plans to investigate additional areas to identify a need for further remedial action for which the Company may be identified as a potentially responsible party and other actions by governmental agencies or private parties.

In the performance of our contracts we routinely request contract modifications that require additional funding from the customer. Most often, these requests are due to customer-directed changes in the scope of work. While we are entitled to recovery of these costs under our contracts, the administrative process with our customer may be protracted. Based on the circumstances, we periodically file requests for equitable adjustment (“REAs”) that are sometimes converted into claims. In some cases, these requests are disputed by our customer. We believe our outstanding modifications, REAs and other claims will be resolved without material impact to our results of operations, financial condition or cash flows.

As a government contractor, with customers including the U.S. government as well as various state and local government entities, the Company may be subject to audits, investigations and claims with respect to its contract performance, pricing, costs, cost allocations and procurement practices. Additionally, amounts billed under such contracts, including direct and indirect costs, are subject to potential adjustments before final settlement.

Management believes that adequate provisions for such potential audits, investigations, claims and contract adjustments, if any, have been made in the financial statements.

Product Warranties

Product warranty costs generally are accrued in proportion to product revenue realized in conjunction with our over-time revenue recognition policy. Product warranty expense is recognized based on the term of the product warranty, generally one year to three years, and the related estimated costs, considering historical claims expense. Accrued warranty costs are reduced as these costs are incurred and as the warranty period expires, and otherwise may be modified as specific product performance issues are identified and resolved. The following is a summary of changes in the product warranty balances during the period ended September 30, 2023:

(Dollars in millions)		
Balance at December 31, 2022	$	18
Additional provision		12
Reversal and utilization		(7)
Balance at September 30, 2023	$	23

Note 15. Related Party Transactions

The Company has related-party sales with the ultimate majority stockholder and its other affiliates that occur in the regular course of business. Related-party sales for these transactions included in revenues were $11 million and $9 million for the three months ended September 30, 2023 and September 30, 2022, respectively, and $24 million and $63 million for the nine months ended September 30, 2023 and September 30, 2022, respectively. The Company has related-party purchases with the ultimate majority stockholder and its other affiliates that occur in the regular course of business. Related-party purchases for these transactions are included in cost of revenues and were $2 million and $2 million for the three months ended September 30, 2023 and September 30, 2022, respectively, and $3 million and $20 million for the nine months ended September 30, 2023 and September 30, 2022, respectively. The receivables related to these transactions with the ultimate majority stockholder and its other affiliates of $15 million and $14 million, respectively, and payables of $3 million and $1 million, respectively, are included in accounts receivable and accounts payable in our Consolidated Balance Sheets as of September 30, 2023 and December 31, 2022. In addition, there was a related-party balance in contract assets of $4 million and $5 million at September 30, 2023 and December 31, 2022, respectively.

Note 16. Segment Information

Operating segments represent components of an enterprise for which separate financial information is available that is regularly reviewed by the CODM in determining how to allocate resources and assess performance. Our Chief Executive Officer is our CODM and he uses a variety of measures to assess the performance of the Company as a whole, depending on the nature of the activity. Beginning in the first quarter of 2022, the Company's operating and reportable segments were revised into two reportable segments, ASC and IMS, to align our market strategy and capital allocation decision making with our operating structure. Prior year information was revised to reflect the new segment structure. All other operations, which consists primarily of DRS corporate headquarters and certain non-operating subsidiaries of the Company, are grouped in Corporate & Eliminations.

We primarily use Adjusted EBITDA, a non-GAAP financial measure, to manage the Company and allocate resources. Adjusted EBITDA of our business segments includes our net earnings before income taxes, amortization of acquired intangible assets, depreciation, restructuring costs, interest, deal related transaction costs, other non-operating expenses such as foreign exchange, the coronavirus pandemic ("COVID-19") response costs, non-service pension expenditures, legal liability accrual reversals, and other one-time non-operational events as well as gains (losses) on business disposals. Adjusted EBITDA is used to facilitate a comparison of the ordinary, ongoing and customary course of our operations on a consistent basis from period to period and provide an additional understanding of factors and trends affecting our business segments. This measure assists the CODM in assessing segment operating performance consistently over time without the impact of our capital structure, asset base and items outside the control of the management team and expenses that do not relate to our core operations.

Certain information related to our segments for the periods ended September 30, 2023 and September 30, 2022 is presented in the following tables. Consistent accounting policies have been applied by all segments within the

Company, within all reporting periods. A description of our reportable segments as of September 30, 2023 and September 30, 2022 has been included in *Note 1: Summary of Significant Accounting Policies*. Intersegment sales are generally transferred at cost to the buying segment, and the sourcing segment does not recognize a profit. Such intercompany operating income is eliminated in consolidation, so that the Company's total revenues and operating earnings reflect only those transactions with external customers.

Total revenues and intersegment revenues by segment for the periods ended September 30, 2023 and September 30, 2022 consists of the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in millions)	2023	2022	2023	2022
ASC	$ 431	$ 408	$ 1,226	$ 1,248
IMS	277	229	692	634
Corporate & Eliminations	(5)	(3)	(18)	(9)
Total revenues	$ 703	$ 634	$ 1,900	$ 1,873

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in millions)	2023	2022	2023	2022
ASC	$ 5	$ 3	$ 18	$ 8
IMS	—	—	—	1
Total intersegment revenues	$ 5	$ 3	$ 18	$ 9

Reconciliation of reportable segment Adjusted EBITDA to Net Earnings (loss) consists of the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in millions)	2023	2022	2023	2022
Adjusted EBITDA				
ASC	$ 48	$ 36	$ 121	$ 125
IMS	34	22	72	73
Corporate & Eliminations	—	—	—	—
Total Adjusted EBITDA	$ 82	$ 58	$ 193	$ 198
Amortization of intangibles	(5)	(3)	(16)	(7)
Depreciation	(16)	(14)	(47)	(41)
Restructuring costs	(2)	—	(10)	—
Interest expense	(10)	(9)	(27)	(27)
Deal related transaction costs	(1)	(16)	(4)	(26)
Gain on sale of business	—	350	—	350
Other one-time non-operational events	—	1	8	—
Income tax provision	(1)	(88)	(3)	(107)
Net earnings	$ 47	$ 279	$ 94	$ 340

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

You should read this discussion together with our Consolidated Financial Statements and related notes thereto included elsewhere in this Quarterly Report.

This discussion and other parts of this Quarterly Report include forward-looking statements such as those relating to our plans, objectives, expectations and beliefs, which involve risks, uncertainties and assumptions. These forward-looking statements are subject to numerous risks and uncertainties, including, but not limited to, the risks and uncertainties discussed under "Special Note Regarding Forward-Looking Statements and Information" and "Risk Factors" in this Quarterly Report and under "Risk Factors" in our annual report on Form 10-K for the year ended December 31, 2022, filed with the SEC on March 28, 2023. Actual results may differ materially from those contained in any forward-looking statements.

Business Overview and Considerations

General

DRS is an innovative and agile provider of advanced defense technology to U.S. national security customers and allies around the world. We specialize in the design, development and manufacture of advanced sensing, network computing, force protection, as well as electric power and propulsion. The strength of our market positioning in these technology areas have created a foundational and diverse base of programs across the Department of Defense ("DoD"). We believe these technologies will not only support our customers in today's mission but will also underpin their strategy to migrate towards more autonomous, dynamic, interconnected, and multi-domain capabilities needed to defend against evolving and emerging threats. We view more advanced capabilities in sensing, computing, self-protection and power as necessary to enable these strategic priorities.

Our overall strategy includes being a balanced and diversified company, less vulnerable to any one budgetary platform or service decision with a specific focus on establishing strong technical and market positions in areas of priority for the DoD. The DoD is our largest customer and for the nine months ended September 30, 2023, accounted for approximately 80% of our business as an end-user, with revenues principally derived directly or indirectly from contracts with the U.S. Army and U.S. Navy, which represented 29% and 40%, respectively, of our total revenues for such period, which is consistent with historic trends.

Our operations and reporting are structured into the following two technology driven segments based on the capabilities and solutions offered to our customers:

Advanced Sensing and Computing

Our Advanced Sensing and Computing ("ASC") segment designs, develops and manufactures sensing and network computing technology that enables real-time situational awareness required for enhanced operational decision making and execution by our customers.

Our sensing capabilities span numerous applications, including missions requiring advanced detection, precision targeting and surveillance sensing, long range electro-optic/infrared ("EO/IR"), signals intelligence ("SIGINT") and other intelligence systems, electronic warfare ("EW"), ground vehicle sensing, next generation active electronically scanned array ("AESA") tactical radars, dismounted soldier sensing and space sensing. Across our offerings, we are focused on advancing sensor distance and enhancing the precision, clarity, definition, spectral depth and effectiveness of our sensors. We also seek to leverage the knowledge and expertise built through our decades of experience to optimize size, weight, power and cost for our customers' specific mission requirements.

Our sensing capabilities are complemented by our rugged, trusted and cyber resilient network computing products. Our network computing offerings are utilized across a broad range of mission applications including platform computing on ground and shipboard (both surface ship and submarine) for advanced battle management, combat systems, radar, command and control ("C2"), tactical networks, tactical computing and communications. These products help support the DoD's need for greater situational understanding at the tactical edge by rapidly transmitting data securely between command centers and forward-positioned defense assets and personnel.

Integrated Mission Systems

Our Integrated Mission Systems ("IMS") segment designs, develops, manufactures and integrates power conversion, control and distribution systems, ship propulsion systems, motors and variable frequency drives, force protection systems, and transportation and logistics systems for the U.S. military and allied defense customers.

DRS is currently a leading provider of next-generation electrical propulsion systems for the U.S. Navy. We provide power conversion, control, distribution and propulsion systems for the Navy's top priority shipbuilding programs, including the Columbia Class ballistic missile submarine, the first modern U.S. electric drive submarine.

We believe DRS is well positioned to meet the needs of an increasingly electrified fleet with our high-efficiency, power dense permanent magnet motors, energy storage systems and associated efficient, rugged and compact power conversion, electrical actuation systems, and advanced cooling technologies.

DRS has a long history of providing a number of other critical products to the U.S. Navy with a significant installed base on submarines, aircraft carriers and other surface ships including motor controllers, instrumentation and control equipment, electrical actuation systems, and thermal management systems for electronics and ship stores refrigeration.

DRS is also an integrator of complex systems in ground vehicles for short-range air defense, counter-unmanned aerial systems ("C-UAS"), and vehicle survivability and protection. Our short-range air defense systems integrate EW equipment, reconnaissance and surveillance systems, modular combat vehicle turrets, and stabilized sensor suites, as well as kinetic countermeasures to protect against evolving threats. Our force protection systems, including solutions for C-UAS and active protection systems on army vehicles help protect personnel and defense assets from enemy combatants.

Focus on Customer and Execution

DRS and its employees focus on our end-customers – the men and women of the armed forces in the U.S. and its allies. We seek to provide high-quality equipment and services to support their mission success. We strive for excellence in everything we do, in every job in our Company, in order to satisfy our customers' needs embedded in our contractual commitments. We seek to ensure that we learn from every lesson experienced in our Company and insist that these lessons affect all elements of our businesses. This approach permeates through the Company with a focus on continuous improvement at every level.

Part of this learning has resulted in institutionalizing our continuous improvement process through our Operational Excellence initiative called "Always Performing For Excellence," or "APEX," program, which is transforming this year from Operational Excellence to Business Excellence. The APEX program's goal is to strive for continuous improvement through unification of all of our business practices, tools and metrics, ongoing employee training and innovation. We believe that excellence is not a destination, but by constantly challenging ourselves to be better, we will improve, and ultimately approach excellence. We challenge ourselves to exceed our customers' expectations and we partner with them to work to ensure that our execution meets their needs.

Continuous improvement through the APEX program also allows us to improve our efficiency, which we believe contributes to increased margins, helps us to remain competitive and allows us to make strategic investments, all while maintaining our focus on customer satisfaction. In these elements, our goals are aligned with those of our customers. We are humbled by the dedication and sacrifice that our ultimate customers have made to serve and we work to perform for them with excellence in everything we do.

Global Events and Business Impacts

COVID-19

The coronavirus pandemic caused certain disruptions to our business, including various adverse supply chain impacts which are anticipated to continue through 2023.

Global Conflicts

In February 2022, Russia escalated its war with Ukraine by invading and occupying parts of that country. Since that time, western powers, including the U.S., have pledged support with humanitarian and military aid. Some of that military aid pledged by the U.S. will result in increased efforts to replace equipment and consumables. We have received orders from the U.S. and allies to both provide equipment in support of this effort, and to replace equipment pledged. We expect that these orders will continue until that support is no longer needed and the equipment pledged is replaced.

In October 2023, Hamas militants located in Gaza launched a terrorist attack on Israel. The ensuing, and ongoing, conflict has the potential to evolve quickly creating uncertainty in the broader Middle East region, along with the potential for disruptions to our Israeli operations in the region, including but not limited to workforce calls for duty, transportation and other logistical impacts and reduced customer confidence. The U.S. and other western powers have indicated military and funding support to Israel. DRS has direct exposure to Israel principally through its RADA operations with approximately 4% of the DRS workforce as of September 30, 2023 residing in Israel. At this time, it is unclear whether supplemental funding for Israel will impact demand for DRS products.

Business Environment

Revenues derived directly, as a prime contractor, or indirectly, as a subcontractor, from contracts with the U.S. government represented 93% and 80% of our consolidated revenue for the three and nine months ended September 30, 2023, respectively, and 83% and 82% of our consolidated revenue for the three and nine months ended September 30, 2022, respectively. Of these sales directly to the U.S. government, the Army and Navy are our largest customers. For the three and nine months ended September 30, 2023, U.S. government sales with the U.S. Army represented 30% and 29% and U.S. government sales with the U.S. Navy represented 48% and 40%, respectively, of our consolidated revenue. For the three and nine months ended September 30, 2022, U.S. government sales with the U.S. Army represented 40% and 35%, respectively, and U.S. government sales with the U.S. Navy represented 31% and 32%, respectively, of our consolidated revenue.

The DoD budget is the largest defense budget in the world.

In March 2023, the U.S. President’s fiscal year 2024 budget request was released and included $842 billion for national defense programs, which marks continued growth from prior years. The most recent National Defense Strategy and annual defense budget request continue to prioritize a strategic focus on China as the pacing threat, countering other near peer adversaries, investing in the nuclear triad, and funding operations in Ukraine. In June 2023, the Fiscal Responsibility Act of 2023 was enacted, which suspends the federal debt ceiling until January 1, 2025, postponing the threat of a federal government default. Pursuant to this law, the President and Congress also agreed upon federal discretionary spending levels for defense and non-defense. For fiscal year 2024, defense spending levels were consistent with the President’s March budget request and reflect an approximately 3% increase over prior levels. For fiscal year 2025, the agreed upon defense spending increase is 1% from prior year levels. However, failure to pass all twelve full year appropriations by calendar year end will trigger 1% cuts from prior year enacted levels. We believe that the strategic priorities requiring more advanced and sophisticated defense technology capabilities create a favorable market environment for DRS.

To prevent a government shutdown at the end of fiscal year 2023, Congress passed a Continuing Resolution (CR) at the end of September, and the President signed the legislation into law on September 30, 2023. The extension is effective through November 17, 2023 allowing lawmakers more time to potentially complete the fiscal year 2024 appropriations bills. In the event of a U.S. government shutdown or an extended period of CR, our business, program performance and results of operations could be impacted by the resulting disruptions to federal government offices, workers, and operations, including but not limited to program cancellations, schedule delays, production halts and other disruptions and nonpayment, which could adversely affect our results of operations. The significance of these impacts will primarily be based on the length of the CR or shutdown.

Operating Performance Assessment and Reporting

For the majority of our contracts, revenues are recognized using the over time, percentage of completion cost-to-cost method of accounting, with revenue recognized based on the ratio of cumulative costs incurred to date to estimated total contract costs at completion. For contracts accounted for in this way, our reported revenues may contain amounts which we have not billed to customers if we have incurred costs, and recognized related profits, in excess of billed progress or performance-based payments.

Under U.S. GAAP, contract costs, including allowable general and administrative expenses on certain government contracts, are charged to work-in-progress inventory and are written off to costs and expenses as revenues are recognized. The Federal Acquisition Regulations (“FAR”) and the defense supplement (“DFARS”), incorporated by reference in U.S. government contracts, provide that internal research and development costs are allowable general and administrative expenses. Unallowable costs, pursuant to the FAR, are excluded from costs accumulated on U.S. government contracts.

Our defense contracts and subcontracts that require the submission of cost or pricing data are subject to audit, various profit and cost controls, and standard provisions for termination at the convenience of the customer. The Defense Contract Audit Agency (“DCAA”) performs these audits on behalf of the U.S. government. The DCAA has the right to perform audits on our incurred costs on cost-type or price redeterminable-type contracts on a yearly basis. Approval of an incurred cost submission can take from one to three years from the date of the submission of the contract cost.

U.S. government contracts are, by their terms, subject to termination by the U.S. government for either convenience or default by the contractor. Fixed-price contracts provide for payment upon termination for items delivered to and accepted by the U.S. government and, if the termination is for convenience, for payment of fair compensation of work performed plus the costs of settling and paying claims by terminated subcontractors, other settlement expenses and a reasonable profit on the costs incurred. Cost-plus contracts provide that, upon termination, the contractor is entitled to reimbursement of its allowable costs and, if the termination is for convenience, a total fee proportionate to the percentage of the work completed under the contract. If a contract termination is for default, however, the contractor is paid an amount agreed upon for completed and partially completed products and services accepted by the U.S. government. In these circumstances, the U.S. government is not liable for excess costs incurred by us in procuring undelivered items from another source.

In addition to the right of the U.S. government to terminate U.S. government contracts, such contracts are conditioned upon the continuing availability of Congressional appropriations. Congress usually appropriates funds for a given program on a September 30 fiscal year basis, even though contract performance may take many years. Consequently, at the outset of a major program, the contract is typically only partially funded, and additional funds normally are committed to the contract by the procuring agency only as appropriations are made by Congress for future fiscal years.

Components of Operations

Revenue

Revenue consists primarily of product related revenue, generating 93% and 93% of our total revenues for the three and nine months ended September 30, 2023, respectively. Our remaining revenue is generated from service related contracts. The percentage of product sales increased from 91% for the three months ended September 30, 2022 to 93% during the current quarter. The increased revenue allocation towards more product based sales is attributed to the disposition of our GES business in August of the 2022 fiscal year. Additionally, 84% and 84% of our revenue is derived from firm-fixed priced contracts for the three and nine months ended September 30, 2023, respectively. This is consistent with the prior year which realized firm-fixed sales of 86% and 87% for the three and nine months ended September 30, 2022, respectively.

Under flexibly priced contracts, we are reimbursed for allowable or otherwise defined total costs (defined as cost of revenues plus allowable general and administrative expenses) incurred, plus a fee. The contracts may also include incentives for various performance criteria, including quality, timeliness, cost-effectiveness or other factors.

For the three and nine months ended September 30, 2023, flexibly priced contracts represented 16% of our total revenues.

Please refer to *Note 3: Revenue from Contracts with Customers* in the Notes to our Consolidated Financial Statements.

Cost of Revenues

Cost of revenues includes materials, labor and overhead costs incurred in the manufacturing, design, and provision of products and services sold in the period as well as warranty costs. Material costs include raw materials, purchased components and sub-assemblies and outside processing and inbound freight. Labor and overhead costs consist of direct and indirect manufacturing costs, including wages and fringe benefits, operating supplies, depreciation and amortization, occupancy costs, and purchasing, receiving, inspection costs and inbound freight costs.

General and Administrative Expenses

General and administrative expenses include general and administrative expenses not included within cost of revenues such as salaries, wages and fringe benefits, facility costs and other costs related to these indirect functions. Additionally, general and administrative expenses include internal research and development costs as well as expenditures related to bid and proposal efforts. We expect general and administrative expenses will continue to be impacted by the costs associated with being a publicly-traded company.

Results from Operations

The following discussion of operating results is intended to help the reader understand the results of operations and financial condition of the Company, for the three and nine months ended September 30, 2023, as compared to the three and nine months ended September 30, 2022. Given the nature of our business, we believe revenue and earnings from operations are most relevant to an understanding of our performance at a business and segment level. Our operating cycle is lengthy and involves various types of production contracts and varying delivery schedules. Accordingly, operating results in a particular period may not be indicative of future operating results.

(Dollars in millions, except per share amounts)	Three Months Ended September 30, 2023	Three Months Ended September 30, 2022	September 30, 2023 vs. September 30, 2022 $	September 30, 2023 vs. September 30, 2022 %
Total revenues	$ 703	$ 634	$ 69	10.9 %
Total cost of revenues	(541)	(504)	(37)	7.3 %
Gross profit	$ 162	$ 130	$ 32	24.6 %
Gross margin	23.0 %	20.5 %	250 bps	
General and administrative expenses	(96)	(101)	5	(5.0)%
Amortization of intangibles	(5)	(3)	(2)	66.7 %
Other operating (expenses) income, net	(2)	350	(352)	(100.6)%
Operating earnings	$ 59	$ 376	$ (317)	(84.3)%
Interest expense	(10)	(9)	(1)	11.1 %
Other, net	(1)	—	(1)	NM
Earnings before taxes	$ 48	$ 367	$ (319)	(86.9)%
Income tax provision	1	88	(87)	(98.9)%
Net earnings	$ 47	$ 279	$ (232)	(83.2)%
Basic EPS(1)	$ 0.18	$ 1.33	$ (1.15)	(86.5)%
Diluted EPS(1)	$ 0.18	$ 1.33	$ (1.15)	(86.5)%
Backlog	$ 4,719	$ 3,138	$ 1,581	50.4 %
Bookings	$ 1,055	$ 874	$ 181	20.7 %

NM- percentage change not meaningful

(1) Gives effect to a 1,450,000-for-1 forward stock split on our common stock effected on February 25, 2021 and a 1.451345331-for-1 forward stock split on our common stock effected November 23, 2022.

(Dollars in millions, except per share amounts)	Nine Months Ended September 30, 2023	Nine Months Ended September 30, 2022	September 30, 2023 vs. September 30, 2022 $	September 30, 2023 vs. September 30, 2022 %
Total revenues	$ 1,900	$ 1,873	$ 27	1.4 %
Total cost of revenues	(1,462)	(1,482)	20	(1.3)%
Gross profit	$ 438	$ 391	$ 47	12.0 %
Gross margin	23.1 %	20.9 %	220 bps	
General and administrative expenses	(286)	(261)	(25)	9.6 %
Amortization of intangibles	(16)	(7)	(9)	128.6 %
Other operating (expenses) income, net	(10)	351	(361)	(102.8)%
Operating earnings	$ 126	$ 474	$ (348)	(73.4)%
Interest expense	(27)	(27)	—	— %
Other, net	(2)	—	(2)	NM
Earnings before taxes	$ 97	$ 447	$ (350)	(78.3)%
Income tax provision	3	107	(104)	(97.2)%
Net earnings	$ 94	$ 340	$ (246)	(72.4)%
Basic EPS[(1)]	$ 0.36	$ 1.62	$ (1.26)	(77.8)%
Diluted EPS[(1)]	$ 0.36	$ 1.62	$ (1.26)	(77.8)%
Backlog	$ 4,719	$ 3,138	$ 1,581	50.4 %
Bookings	$ 2,502	$ 2,304	$ 198	8.6 %

NM- percentage change not meaningful

(1) Gives effect to a 1,450,000-for-1 forward stock split on our common stock effected on February 25, 2021 and a 1.451345331-for-1 forward stock split on our common stock effected November 23, 2022.

Revenue

Our revenue generation of $703 million for the three months ended September 30, 2023 represents an increase of $69 million or 10.9% as compared to the three months ended September 30, 2022. The revenue increase is primarily attributed to continued performance on our electric power and propulsion programs with the U.S. Navy which was offset in part by a reduction in Force Protection related revenues, both within our IMS segment, during the period.

Our revenue generation of $1,900 million for the nine months ended September 30, 2023 represents an increase of $27 million or 1.4% over the nine months ended September 30, 2022. The revenue increase was also driven by increased demand within our electric power and propulsion programs with the U.S. Navy for both submarine and surface ships within our IMS segment. This was offset in part by the difference in revenue contribution realized from our now disposed Global Enterprise Solutions ("GES") operating unit as compared to the revenue generated from RADA, the "net divestiture impact."

Cost of Revenues

Cost of revenues increased by $37 million or 7.3% from $504 million to $541 million for the three months ended September 30, 2023 as compared to the three months ended September 30, 2022. The cost of revenue increase was primarily due to the increased revenue contribution realized during the period. This was offset in part by improved program performance within our laser sensing portfolio as well as the mix benefit realized from increased sales of our tactical radars acquired in the RADA acquisition. In total for the three months ended September 30, 2023, cost of revenues decreased as a percentage of revenues driving gross margin contribution to 23.0% as compared to 20.5% realized during the three months ended September 30, 2022.

Cost of revenue decreased by $20 million or 1.3% from $1,482 million to $1,462 million for the nine months ended September 30, 2023 as compared to the nine months ended September 30, 2022. The decrease was primarily due to the reduced cost of revenues attributed to favorable program mix and performance within both our IMS and ASC segments highlighted by the continued performance improvements realized within our laser program portfolio. Additionally the higher profit generation of the RADA revenue contribution further drove a reduction in the overall cost of revenues. For the year to date period, this was partially offset by the reduction of revenues noted above as well as certain programmatic cost growth realized on our dismounted soldier sensing programs.

Gross Profit

Gross profit increased by $32 million, or 24.6% to $162 million for the three months ended September 30, 2023 as compared to $130 million for the three months ended September 30, 2022, and gross profit increased by $47 million or 12.0% for the nine months ended September 30, 2023 as compared to the nine months ended September 30, 2022 resulting from the revenue and cost of revenue trends noted above.

General and Administrative Expenses

General and administrative expenses (“G&A”) decreased by $5 million or 5.0% for the three months ended September 30, 2023 as compared to the three months ended September 30, 2022 and increased by $25 million or 9.6% for the nine months ended September 30, 2023 as compared to the nine months ended September 30, 2022. The decrease in G&A for the three months ended September 30, 2023 is primarily attributed to transaction costs recorded in 2022, partially offset by increased investment in internal research and development (“IR&D”) of $2 million and public company operating costs. The increase in G&A for the nine months ended September 30, 2023 is primarily due to increased investment in IR&D expenditures of $18 million, the addition of the RADA commercial business model and increased public company operating costs also contributed to the year over year increase in G&A expenditures.

Amortization of Intangibles

Amortization of intangibles of $5 million for the three months ended September 30, 2023 increased $2 million as compared to the three months ended September 30, 2022. Amortization of intangibles of $16 million for the nine months ended September 30, 2023 increased $9 million as compared to the nine months ended September 30, 2022. This is attributed to the increased amortization generated from the RADA acquired intangible assets.

Other Operating (Expenses) Income, Net

Other operating (expenses) income decreased from an income of $350 million and $351 million for the three and nine months ended September 30, 2022, respectively, to an expense of $2 million and $10 million for the three and nine months ended September 30, 2023, respectively. The income for both the three and nine months in the prior year is primarily due to the gain on sale of the GES business and AAC Joint venture which totaled $350 million. The expense in the current year is largely attributed to restructuring efforts implemented in our ASC segment.

Operating Earnings

Operating earnings decreased by $317 million to $59 million for the three months ended September 30, 2023. For the nine months ended September 30, 2023, operating earnings decreased by $348 million from $474 million for nine months ended September 30, 2022 to $126 million for the nine months ended September 30, 2023. The decrease was driven by the gains on asset sales in the prior year, resulting from our dispositions of our GES and AAC operating units.

Interest Expense

Interest expense remained relatively consistent realizing an expense of $10 million for three months ended September 30, 2023, compared to $9 million for the three months ended September 30, 2022. For the nine months ended September 30, 2023 and September 30, 2022, interest expense remained consistent at $27 million.

Other, Net

Other, net increased $1 million for the three months ended September 30, 2023 when compared to the three months ended September 30, 2022, and increased $2 million for the nine months ended September 30, 2023 when compared to the nine months ended September 30, 2022.

Earnings Before Taxes

Earnings before taxes decreased by $319 million and $350 million to $48 million and $97 million for the three and nine months ended September 30, 2023, respectively, from $367 million and $447 million for the three and nine months ended September 30, 2022, respectively. This was primarily due to the decreases in operating earnings as noted above.

Income Tax Provision

Income tax provision decreased by $87 million and $104 million to $1 million and $3 million for the three and nine months ended September 30, 2023, respectively, from $88 million and $107 million for the three and nine months ended September 30, 2022, respectively. This was primarily attributable to the prior year tax expenditures on the gains realized on the disposition of GES and AAC in the prior year. This was compounded by the federal research and development credits recorded in the three and nine months ended September 30, 2023, which further reduced our tax expenditures for the three and nine months ended September 30, 2023.

Net Earnings

Net earnings decreased by $232 million to $47 million for the three months ended September 30, 2023 and decreased $246 million to $94 million for the nine months ended September 30, 2023, respectively, when compared to the three and nine months ended September 30, 2022. This was driven by a decrease in earnings before taxes offset by the income tax provision decreasing as noted above.

Backlog

Backlog - We define Backlog to include the following components:

(1) Funded - Funded backlog represents the revenue value of orders for services under existing contracts for which funding is appropriated or otherwise authorized less revenue previously recognized on these contracts.

(2) Unfunded - Unfunded backlog represents the revenue value of firm orders for products and services under existing contracts for which funding has not yet been appropriated less funding previously recognized on these contracts.

Total backlog increased by $1,581 million to $4,719 million for nine months ended September 30, 2023, from $3,138 million for the nine months ended September 30, 2022. The backlog increase was driven primarily by the receipt of a multi-boat contract to support the electric propulsion efforts on the Columbia Class submarine program with the U.S. Navy. Subsequent to the third quarter, the Company agreed to contract terms and pricing totaling over $3 billion, for the majority of our electric power and propulsion system on the remaining seven Columbia Class submarines. The award is not included in the backlog numbers noted above.

Bookings

Bookings - We define bookings as the total value of contract awards received from the U.S. government for which it has appropriated funds and legally obligated such funds to the Company through a contract or purchase order, plus the value of contract awards and orders received from customers other than the U.S. government.

Bookings results for three months ended September 30, 2023 increased to $1,055 million as compared to $874 million for the three months ended September 30, 2022. Bookings for the nine months ended September 30, 2023 increased by 9% or $198 million to $2,502 million as compared to $2,304 million for the nine months ended September 30, 2022.

Key Non-GAAP Operating Measures

Overview

We measure our business using both key financial and operating data including key performance indicators ("KPIs") and non-GAAP financial measures. In addition to the operational analysis detailed above, we also use the following non-GAAP metrics to manage our business, monitor results of operations and ensure proper allocation of capital: (i) Adjusted EBITDA, (ii) Adjusted EBITDA Margin, (iii) Adjusted Diluted Earnings Per Share ("EPS") and (iv) Free Cash Flow. We believe that these financial performance metrics represent the primary drivers of value enhancement, balancing both short and long-term indicators of increased shareholder value. These are the metrics we use to measure our results and evaluate our business and related contract performance.

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in millions, except per share amounts)	2023	2022	2023	2022
Adjusted EBITDA[1]	$ 82	$ 58	$ 193	$ 198
Adjusted EBITDA Margin[1]	11.7%	9.2%	10.2%	10.6%
Adjusted Diluted EPS[1][2]	$ 0.20	$ 0.12	$ 0.42	$ 0.47
Free Cash Flow[1]			$ (335)	$ (262)

(1) Note on non-GAAP financial measures: Throughout the discussion of our results of operations we use non-GAAP financial measures including Adjusted EBITDA, Adjusted EBITDA Margin, Adjusted Diluted EPS and Free Cash Flow, as measures of our overall performance. Definitions and reconciliations of these measures to the most directly comparable financial measure calculated and presented in accordance with U.S. GAAP are included below.

(2) Gives effect to a 1,450,000-for-1 forward stock split on our common stock effected on February 25, 2021 and a 1.451345331-for-1 forward stock split on our common stock effected November 23, 2022.

Non-GAAP Financial Measures

We believe the non-GAAP financial measures presented in this document will help investors understand our financial condition and operating results and assess our future prospects. We believe these non-GAAP financial measures, each of which is discussed in greater detail below, are important supplemental measures because they exclude unusual or non-recurring items as well as non-cash items that are unrelated to or may not be indicative of our ongoing operating results. Further, when read in conjunction with our U.S. GAAP results, these non-GAAP financial measures provide a baseline for analyzing trends in our underlying businesses and can be used by management as a tool to help make financial, operational and planning decisions. Finally, these measures are often used by analysts and other interested parties to evaluate companies in our industry by providing more comparable measures that are less affected by factors such as capital structure.

We recognize that these non-GAAP financial measures have limitations, including that they may be calculated differently by other companies or may be used under different circumstances or for different purposes, thereby affecting their comparability from company to company. In order to compensate for these and the other limitations discussed below, management does not consider these measures in isolation from or as alternatives to the comparable financial measures determined in accordance with U.S. GAAP. Readers should review the reconciliations below and should not rely on any single financial measure to evaluate our business.

We define these non-GAAP financial measures as:

Adjusted EBITDA and Adjusted EBITDA Margin

We define Adjusted EBITDA as our net earnings before income taxes, amortization of acquired intangible assets, depreciation, restructuring costs, interest, deal related transaction costs, other non-operating expenses such as foreign exchange, COVID-19 response costs, non-service pension expenditures, legal liability accrual reversals, and other one-time non-operational events as well as gains (losses) on business disposals. Adjusted EBITDA Margin is calculated by dividing Adjusted EBITDA by revenue. Adjusted EBITDA and Adjusted EBITDA Margin are not measures calculated in accordance with U.S. GAAP, and they should not be considered an alternative to any financial measures that were calculated under U.S. GAAP. Adjusted EBITDA and Adjusted EBITDA Margin are used to facilitate a comparison of the ordinary, ongoing and customary course of our operations on a consistent basis from period to period and provide an additional understanding of factors and trends affecting our business. Adjusted EBITDA and Adjusted EBITDA Margin are driven by changes in volume, performance, contract mix and general and administrative expenses and investment levels. Performance, as used in this definition, refers to changes in profitability and is primarily based on adjustments to estimates at completion on individual contracts. These adjustments result from increases or decreases to the estimated value of the contract, the estimated costs to complete the contract, or both. These measures therefore assist management and our board and may be useful to investors in comparing our operating performance consistently over time as they remove the impact of our capital structure, asset base and items outside the control of the management team and expenses that do not relate to our core operations. Adjusted EBITDA and Adjusted EBITDA Margin may not be comparable to similarly titled non-GAAP measures used by other companies as other companies may have calculated the measures differently. The reconciliation of Adjusted EBITDA to net earnings is provided below:

Consolidated Entity Adjusted EBITDA Reconciliation:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in millions)	2023	2022	2023	2022
Net earnings	$ 47	$ 279	$ 94	$ 340
Income tax provision	1	88	3	107
Amortization of intangibles	5	3	16	7
Depreciation	16	14	47	41
Restructuring costs	2	—	10	—
Interest expense	10	9	27	27
Deal related transaction costs	1	16	4	26
Gain on sale of business	—	(350)	—	(350)
Other one-time non-operational events	—	(1)	(8)	—
Adjusted EBITDA	$ 82	$ 58	$ 193	$ 198
Adjusted EBITDA Margin	11.7%	9.2%	10.2%	10.6%

Adjusted EBITDA

Adjusted EBITDA increased by $24 million or 41.4% to $82 million for the three months ended September 30, 2023 compared to the three months ended September 30, 2022. The increase in Adjusted EBITDA for the three month period is primarily attributed to improved program performance noted above offset by increased IR&D investments and the impact of higher public company expenditures both residing in our G&A expense line item. For the nine months ended September 30, 2023, Adjusted EBITDA decreased $5 million or 2.5% to $193 million from $198 million for the nine months ended September 30, 2022. This is primarily attributed to the increase in IR&D and public company expenditures as well as the non- recurring 'one-time' increase in profitability on the Columbia Class program experienced in the nine months ended September 30, 2022.

Adjusted EBITDA Margin

Adjusted EBITDA Margin was 9.2% and 10.6% for the three and nine months ended September 30, 2022, respectively, and 11.7% and 10.2% for the three and nine months ended September 30, 2023, respectively. The increase for the quarter was primarily due to operational leverage realized on the 10.9% increase in revenue realized during the three months ended September 30, 2023 as compared to the three month period ended September 30, 2022. This was compounded by improved program performance further enhancing our adjusted EBITDA margin.

The decrease for the nine month period was primarily due to the increased G&A expenditures as well as the 'one-time' non-recurring profitability on the Columbia Class program mentioned above.

Adjusted Diluted EPS

Adjusted Diluted EPS – We calculate Adjusted Diluted EPS by excluding deal related transaction costs, amortization of acquired intangible assets, restructuring costs, other non-operating expenses such as foreign exchange, COVID-19 response costs, non-service pension expenditures, legal liability accrual reversals, and other one-time non-operational events as well as gains (losses) on business disposals (net of taxes) from our net earnings and dividing by the diluted weighted average number of shares outstanding to arrive at Adjusted Diluted EPS. We believe that Adjusted Diluted EPS allows investors to effectively compare our core performance from period to period by excluding items that are not indicative of, or are unrelated to, results from our ongoing business. Adjusted Diluted EPS has limitations as an analytical tool and does not represent and should not be considered an alternative to basic or diluted EPS as determined in accordance with U.S. GAAP. The reconciliation of Adjusted Diluted EPS to U.S. GAAP diluted EPS is shown below:

Consolidated Entity Reconciliation of Adjusted Diluted EPS:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in millions, except per share amounts; shares in millions)	**2023**	**2022**	**2023**	**2022**
Net earnings	$ 47	$ 279	$ 94	$ 340
Deal related transaction costs	1	16	4	26
Amortization of intangibles	5	3	16	7
Restructuring costs	2	—	10	—
Gain on sale of business, net of taxes	—	(270)	—	(270)
Other one-time non-operational events	—	(1)	(8)	—
Tax effect of adjustments	(2)	(2)	(5)	(5)
Adjusted net earnings	$ 53	$ 25	$ 111	$ 98
Diluted weighted average number of shares outstanding	265	210	264	210
Diluted EPS[(1)]	$ 0.18	$ 1.33	$ 0.36	$ 1.62
Adjusted diluted EPS[(1)]	$ 0.20	$ 0.12	$ 0.42	$ 0.47

(1) Gives effect to a 1,450,000-for-1 forward stock split on our common stock effected on February 25, 2021 and a 1.451345331-for-1 forward stock split on our common stock effected November 23, 2022.

Adjusted Diluted EPS

For the nine months ended September 30, 2023 there were 262,039,337 shares of common stock outstanding, an increase of 51,594,264 shares from the September 30, 2022 shares outstanding of 210,445,073. The increased share count is attributed to shares issued to consummate the RADA merger of 49,788,960 and equity vesting and stock option exercises of 1,805,304. Diluted shares as of September 30, 2023 totaled 3 million and 3 million for the three and nine months ended September 30, 2023, respectively, increasing from the prior year which predated equity award grants. The diluted shares are attributable to equity grants and unexercised stock options. There were no outstanding equity grants at September 30, 2022. Adjusted diluted EPS of $0.20 for the three months ended September 30, 2023 increased $0.08 as compared with the same period in the prior year. The increase is a product of the increased adjusted net earnings offset by the increased share count as noted above. Adjusted Diluted EPS of $0.42 for the nine months ended September 30, 2023 represents a decrease of $0.05 from $0.47 for the nine months ended September 30, 2022, which is attributed to the increase in shares outstanding noted above, partially offset by the adjusted net earnings increase as shown in the table above.

Free Cash Flow

Free Cash Flow – We define free cash flow as the sum of the cash flows provided by (used in) operating activities, the cash flows provided by (used in) investing activities pertaining to capital expenditures, and proceeds generated from the sale of capital assets, less transaction related expenditures (net of tax).

We believe that free cash flow provides management and investors with an important measure of our ability to generate cash on a normalized basis. Free cash flow also provides insight into our flexibility to allocate capital and pursue opportunities that may enhance stockholder value. We believe that while expenditures and dispositions of property, plant and equipment will fluctuate period to period, we seek to ensure that we have adequate capital on hand to maintain ongoing operations and enable growth of the business. Additionally, free cash flow is of limited usefulness, in that it does not represent residual cash flows available for discretionary expenditures, due to the fact the measures do not deduct the payments required for debt service and other contractual obligations or payments. The reconciliation between free cash flow and net cash provided by operating activities (the most comparable U.S. GAAP measure) is shown below:

Consolidated Entity Reconciliation of Free Cash Flow:

	Nine Months Ended September 30,	
(Dollars in millions)	**2023**	**2022**
Net cash used in operating activities	$ (310)	$ (246)
Transaction related expenditures, net of tax	17	19
Capital expenditures	(42)	(35)
Proceeds from sales of assets	—	—
Free cash flow	$ (335)	$ (262)

Free Cash Flow

Free cash flow usage increased by $73 million to $335 million for the nine months ended September 30, 2023 from $262 million for the nine months ended September 30, 2022. This was primarily due to cash used to fund working capital for the nine months ended September 30, 2023 when compared to nine months ended September 30, 2022.

Factors Impacting Our Performance

U.S. Government Spending and Federal Budget Uncertainty

Changes in the volume and relative mix of U.S. government spending as well as areas of spending growth could impact our business and results of operations. In particular, our results can be affected by shifts in strategies and priorities on homeland security, intelligence, defense-related programs, infrastructure and urbanization and continued increased spending on technology and innovation, including cybersecurity with respect to our and third parties' information networks and related systems, artificial intelligence, connected communities and physical infrastructure (for example, the potential impacts for the Russia / Ukraine conflict and the Israel-Hamas war). Cost-cutting and efficiency initiatives, current and future budget restrictions, spending cuts and other efforts to reduce government spending and shifts in overall priorities could cause our government customers to reduce or delay funding or invest appropriated funds on a less consistent basis or not at all, and demand for our solutions or services could diminish. Furthermore, any disruption in the functioning of government agencies, including as a result of government closures and shutdowns, could have a negative impact on our operations and cause us to lose revenue or incur additional costs due to, among other things, our inability to maintain access and schedules for government testing or deploy our staff to customer locations or facilities as a result of such disruptions.

There is also uncertainty around the timing, extent, nature and effect of Congressional and other U.S. government actions to address budgetary constraints, caps on the discretionary budget for defense and non-defense departments and agencies, and the ability of Congress to determine how to allocate the available budget authority and pass appropriations bills to fund both U.S. government departments and agencies that are, and those that are not, subject to the caps. Additionally, budget deficits and the growing U.S. national debt, may increase pressure on the U.S. government to reduce federal spending across all federal agencies, with uncertainty about the size and timing of those reductions. Furthermore, delays in the completion of future U.S. government budgets could in the future delay procurement of the federal government services we provide. A reduction in the amount of, or reductions, delays, or cancellations of funding for, services that we are contracted to provide to the U.S. government as a result of any of these impacts or related initiatives, legislation or otherwise could have a material adverse effect on our business and results of operations. See Part I, Item 1A, "Risk Factors—Risks Related to Our Business—Significant delays or reductions in appropriations for our programs and changes in U.S. government priorities and spending levels more broadly may negatively impact our business and could have a material adverse impact on our business, financial condition and results of operations" Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations—Business Overview and Considerations—Business Environment" in our Annual Report for the year ended December 31, 2022, filed with the SEC on March 28, 2023 and Part I, Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations—Business Overview and Considerations—Business Environment" in this Quarterly Report for further details on U.S. government spending's impact on our business.

Operational Performance on Contracts

The Company recognizes revenue for each separately identifiable performance obligation in a contract representing an obligation to transfer a distinct good or service to a customer. In most cases, goods and services provided under the Company's contracts are accounted for as single performance obligations due to the complex and integrated nature of our products and services. These contracts generally require significant integration of a group of goods and/or services to deliver a combined output. In some contracts, the Company provides multiple distinct goods or services to a customer. In those cases, the Company accounts for the distinct contract deliverables as separate performance obligations and allocates the transaction price to each performance obligation based on its relative standalone selling price, which is generally estimated using cost plus a reasonable margin. We classify revenues as products or services on our Consolidated Statements of Earnings based on the predominant attributes of the performance obligations. While the Company provides warranties on certain contracts, we typically do not provide for services beyond standard assurances and therefore do not consider warranties to be separate performance obligations. Typically, we enter into three types of contracts: fixed-price contracts, cost-plus contracts and T&M contracts (cost-plus contracts and T&M contracts are aggregated below as flexibly priced contracts). The majority of our total revenues are derived from fixed-price contracts; refer to the revenue disaggregation disclosures in *Note 3: Revenue from Contracts with Customers*.

For fixed-price contracts, customers agree to pay a fixed amount, negotiated in advance for a specified scope of work.

For cost-plus contracts typically we are reimbursed for allowable or otherwise defined total costs (defined as cost of revenues plus allowable general and administrative expenses) incurred, plus a fee. The contracts may also include incentives for various performance criteria, including quality, timeliness and cost-effectiveness. In addition, costs are generally subject to review by clients and regulatory audit agencies, and such reviews could result in costs being disputed as non-reimbursable under the terms of the contract.

T&M contracts provide for reimbursement of labor hours expended at a contractual fixed labor rate per hour, plus the actual costs of material and other direct non-labor costs. The fixed labor rates on T&M contracts include amounts for the cost of direct labor, indirect contract costs and profit.

Revenue from contracts with customers is recognized when the performance obligations are satisfied through the transfer of control over the good or service to the customer, which may occur either over time or at a point in time.

Revenues for the majority of our contracts are measured using the over time, percentage of completion cost-to-cost method of accounting to calculate percentage of completion. We believe this is an appropriate measure of progress toward satisfaction of performance obligations as this measure most accurately depicts the progress of our work and transfer of control to our customers. Due to the long-term nature of many of our contracts, developing the estimated total cost at completion and total transaction price often requires judgment. Factors that must be considered in estimating the cost of the work to be completed include the nature and complexity of the work to be performed, subcontractor performance and the risk and impact of delayed performance.

After establishing the estimated total cost at completion, we follow a standard Estimate at Completion ("EAC") process in which we review the progress and performance on our ongoing contracts. The following represents the impact that changes in our estimates, particularly those regarding our fixed-price development programs, have had on our revenues for the three and nine months ended September 30, 2023 and 2022, respectively:

Impact of Change in Estimates on our Revenue Results:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in millions)	2023	2022	2023	2022
Revenue	$ 6	$ (11)	$ (14)	$ (22)
Total % of Revenue	0.9 %	1.8 %	0.7 %	1.2 %

Additionally, the timing of our cash flows is impacted by the timing of achievement of billable milestones on contracts. Historically, this has resulted and could continue to result in fluctuations in working capital levels and quarterly free cash flow results. As a result of such quarterly fluctuations in free cash flow results, we believe that quarter-to-quarter comparisons of our results of operations may not necessarily be meaningful and should not be relied upon as indicators of future performance.

Regulations

Increased audit, review, investigation and general scrutiny by U.S. government agencies of performance under government contracts and compliance with the terms of those contracts and applicable laws could affect our operating results. Negative publicity and increased scrutiny of government contractors in general, including us, relating to government expenditures for contractor services and incidents involving the mishandling of sensitive or classified information as well as the increasingly complex requirements of the DoD and the U.S. intelligence community, including those related to cybersecurity, could impact our ability to perform in the markets we serve.

International & Commercial Sales

International revenue, including foreign military sales, foreign military financing, and direct commercial sales, accounted for approximately 7% and 20% of our revenue for the three and nine months ended September 30, 2023, respectively, and 17% and 18% of our revenues for the three and nine months ended September 30, 2022, respectively. The increase is due in part to increased purchases resulting from continued military aid programs in support of Ukraine in its conflict with Russia. Given that our focus is primarily with the DoD and our investments are focused as such, we anticipate that international sales will continue to account for a similar percentage of revenue in the future. We remain subject to the spending levels, pace and priorities of the U.S. government as well as international governments and commercial customers, and to general economic conditions that could adversely affect us, our customers and our suppliers.

Additionally, some international sales may expose us to foreign exchange fluctuations and changing dynamics of foreign competitiveness based on variations in the value of the U.S. dollar relative to other currencies. The impact of those fluctuations is reflected throughout our Consolidated Financial Statements, but in the aggregate, did not have a material impact on our results of operations for three and nine months ended September 30, 2023.

Acquisitions

We consider the acquisition of businesses and investments that we believe will expand or complement our current portfolio and allow access to new customers or technologies. We also may explore the divestiture of businesses that no longer meet our needs or strategy or that could perform better outside of our organization.

On November 28, 2022, the Company announced the successful completion of the all-stock merger between Leonardo DRS and RADA, a leading Israel-based provider of small-form tactical radar, to become a combined public company. As previously disclosed, RADA shareholders retained approximately 19% ownership in the combined Company with Leonardo DRS's parent company, Leonardo S.p.A., (MIL: LDO), owning the remaining 81%. Immediately following the closing, the Company began trading on the Nasdaq Stock Exchange and the Tel Aviv Stock Exchange under the ticker "DRS."

The acquisition of RADA has been accounted for using the acquisition method of accounting in accordance with ASC 805, *Business Combinations,* with the Company as the accounting acquirer, which requires the assets acquired and liabilities assumed be recognized at their acquisition date fair value. The acquisition was completed on November 28, 2022, when each issued and outstanding ordinary share of RADA was converted and exchanged for one share of common stock of the Company.

The total purchase consideration for RADA was $511 million and is comprised of the Company's shares issued in exchange for all issued and outstanding common shares of RADA, as well as the portion of replacement stock compensation awards' fair value attributable to pre-combination services. See *Note 2: Business Acquisitions and Dispositions* for additional information regarding the transaction.

Dispositions

On March 21, 2022, the Company entered into a definitive agreement to sell its Global Enterprise Solutions ("GES") business to SES Government Solutions, Inc., a wholly-owned subsidiary of SES S.A., for $450 million subject to certain working capital adjustments. The transaction was completed on August 1, 2022 and resulted in cash proceeds of $427 million after net working capital adjustments. The transaction netted an aggregate pretax gain net of transaction costs of $309 million ($239 million after tax) of which $323 million was included in Other Operating income (expense) net partially reduced by aggregate transaction costs of $14 million included in Selling, General & Administrative costs and tax expenses of $70 million. GES, which was part of the ASC segment, provides commercial satellite communications to the U.S. Government and delivers satellite communications and security solutions to customers worldwide.

The Company recorded operating income for the GES business of $13 million and $29 million for the years ended December 31, 2022 and 2021, respectively.

On April 19, 2022, we entered into a definitive sales agreement to divest our share of our equity investment in Advanced Acoustic Concepts LLC ("AAC") for $56 million to Thales Defense & Security, Inc., the minority partner in AAC. The transaction was completed on July 8, 2022 and resulted in proceeds of $56 million. The transaction netted an aggregate pretax gain of $31 million ($22 million net of taxes). The aggregate gain of $31 million is included in Other Operating income (expense) net offset by tax expense of $9 million.

The proceeds generated from the GES and AAC divestitures resulted in a $396 million dividend to US Holding, at that time, our sole stockholder. The $396 million represents the proceeds generated net of our costs to sell and estimated tax obligations. The dividend was issued on August 5, 2022.

Review of Operating Segments

The following is a discussion of operating results for each of our operating segments. We have elected to use Revenue, Adjusted EBITDA, Adjusted EBITDA Margin, and Bookings to provide detailed information on our segment performance. Additional information regarding our segments can be found in *Note 16: Segment Information* within the unaudited Consolidated Financial Statements.

	Three Months Ended September 30,		September 30, 2023 vs. September 30, 2022 Variance	
(Dollars in millions)	2023	2022		
Revenues:				
ASC	$ 431	$ 408	$ 23	5.6 %
IMS	277	229	48	21.0 %
Corporate & Eliminations	(5)	(3)	(2)	66.7 %
Total revenues	$ 703	$ 634	$ 69	10.9 %
Adjusted EBITDA:				
ASC	$ 48	$ 36	$ 12	33.3 %
IMS	34	22	12	54.5 %
Corporate & Eliminations	—	—	—	NM
Total Adjusted EBITDA	$ 82	$ 58	$ 24	41.4 %
Adjusted EBITDA Margin:				
ASC	11.1 %	8.8 %	230 bps	
IMS	12.3 %	9.6 %	270 bps	
Bookings:				
ASC	$ 820	$ 700	$ 120	17.1 %
IMS	235	174	61	35.1 %
Total bookings	$ 1,055	$ 874	$ 181	20.7 %

	Nine Months Ended September 30,		September 30, 2023 vs. September 30, 2022 Variance	
(Dollars in millions)	2023	2022		
Revenues:				
ASC	$ 1,226	$ 1,248	$ (22)	(1.8)%
IMS	692	634	58	9.1 %
Corporate & Eliminations	(18)	(9)	(9)	100.0 %
Total revenues	$ 1,900	$ 1,873	$ 27	1.4 %
Adjusted EBITDA:				
ASC	$ 121	$ 125	$ (4)	(3.2)%
IMS	72	73	(1)	(1.4)%
Corporate & Eliminations	—	—	—	NM
Total Adjusted EBITDA	$ 193	$ 198	$ (5)	(2.5)%
Adjusted EBITDA Margin:				
ASC	9.9 %	10.0 %	(10) bps	
IMS	10.4 %	11.5 %	(110) bps	
Bookings:				
ASC	$ 1,693	$ 1,573	$ 120	7.6 %
IMS	809	731	78	10.7 %
Total bookings	$ 2,502	$ 2,304	$ 198	8.6 %

ASC

Revenue:

The ASC segment reported revenue of $431 million and $1,226 million for the three and nine months ended September 30, 2023, respectively, an increase of 6% or $23 million from the three months ended September 30,

2022. The increase is attributed to Naval and Land based network computing programs. This was offset in part by a reduction in international dismounted soldier programs realized during the period.

The ASC segment realized a revenue decrease of 2% or $22 million from the nine months ended September 30, 2022. This decrease is attributed to the net divestiture impact, in which our disposed assets (GES) provided a higher revenue contribution than the acquired RADA asset for the year to date period. The net divestiture impact was offset in large part by increased revenue contributions within our airborne sensing and naval computing programs.

Adjusted EBITDA and Adjusted EBITDA Margin:

ASC's Adjusted EBITDA increased by $12 million or 33% to $48 million from $36 million for the three months ended September 30, 2023 when compared to the three months ended September 30, 2022. The increase was driven by increased revenue contribution, favorable mix and improved program performance. This was offset by an increase in G&A expenditures attributed to IR&D investments, incremental public company costs allocated to the segment, as well as the increased G&A attributed to the RADA commercial business model.

For the nine month period ended September 30, 2023 Adjusted EBITDA decreased $4 million or 3%, from $125 million to $121 million. The decrease in Adjusted EBITDA was driven by increased G&A expenditures attributed to IR&D investments, incremental public company costs allocated to the segment, as well as the increased G&A attributed to the RADA commercial business model. Additionally the ASC segment realized a reduction in revenue as compared to the prior nine month period ended September 30, 2022. These reductions were offset by increased gross margin contribution attributed in large part to the high margin realized on the RADA revenue contribution.

The increase in Adjusted EBITDA drove an increase in Adjusted EBITDA Margin from 8.8% for the three months ended September 30, 2022 to 11.1% for the three months ended September 30, 2023. The margin expansion is driven by the incremental revenue contribution during the period coupled with improved program performance as noted above. The increase was offset in part by the incremental G&A investments detailed above.

ASC realized a decrease in Adjusted EBITDA which drove a slight decrease in Adjusted EBITDA Margin from 10.0% for the nine months ended September 30, 2022 to 9.9% for nine months ended September 30, 2023. The margin impact was attributed to the reduction in operational leverage from the reduction in revenues attributed to the net divestiture impact coupled with the increase in G&A expenditures as noted above. This was largely offset by the improved program performance and higher margin contribution from the RADA tactical radar sales.

Bookings:

The ASC segment generated a 17.1% increase in bookings for the three months ended September 30, 2023 increasing $120 million when compared to the three months ended September 30, 2022. The increase in new awards is driven by increased demand for ground vehicle and airborne sensing programs. Bookings continue to exceed the revenue output driving an increase in backlog over the period.

For the nine months ended September 30, 2023 bookings also increased $120 million or 7.6% from the nine months ended September 30, 2022, driving a total booking contribution of $1,693 million for the current period. The increase is driven by ground vehicle sensing and naval computing programs awarded during the period.

IMS

Revenue:

IMS segment revenue increased by $48 million or 21% to $277 million for the three months ended September 30, 2023 from $229 million for the three months ended September 30, 2022 attributed to continued momentum in our naval power and propulsion business. Additionally, the trend continued in the nine months ended September 30, 2023 with revenue growth of $58 million or 9% to $692 million for the nine months ended September 30, 2023 from $634 million for the nine months ended September 30, 2022. The growth for the nine month period was also attributed to our naval power and propulsion business but was partially offset by the non-recurring impact of the contract modification on the Columbia program realized in the prior year.

Adjusted EBITDA and Adjusted EBITDA Margin:

IMS's Adjusted EBITDA increased by $12 million or 55% to $34 million for the three months ended September 30, 2023 from $22 million for the three months ended September 30, 2022. The increase for the quarter is attributed to operational leverage created by the increased revenue output as well as continued program improvement on our Columbia Class submarine program. This drove Adjusted EBITDA margin up 270 bps to 12.3% compared to the 9.6% realized during the three month period ended September 30, 2022.

For the nine months ended September 30, 2023, Adjusted EBITDA decreased $1 million or 1% to $72 million from $73 million for the nine months ended September 30, 2022. This was primarily due to the favorable financial impact realized from the 2nd ship-set contract modification on the Columbia program realized in the first quarter of 2022 ($25 million) largely offset by increased revenue contribution and the related operational leverage.

Bookings:

Booking contributions increased by $61 million and $78 million or 35.1% and 10.7% for the three and nine months ended September 30, 2023, respectively, to $235 million and $809 million from $174 million and $731 million for the three and nine months ended September 30, 2022, respectively. The increase for the quarter is largely attributed to our force protection efforts in short range air defense and logistic support programs. For the year to date period the bookings performance is largely attributed to continued funding progress on our Electronic Power & Propulsion contracts.

Liquidity and Capital Resources

We endeavor to ensure the most efficient conversion of operating income into cash for deployment in our business and to maximize stockholder value through cash deployment activities. In addition to our cash position, we use various financial measures to assist in capital deployment decision-making, including cash provided by operating activities and free cash flow, a non-GAAP measure described in more detail below. We believe that the combination of our existing cash, access to credit facilities as described in *Note 11: Debt* and future cash that we expect to generate from our operations will be sufficient to meet our short and long-term liquidity needs. There can be no assurance, however, that our business will continue to generate cash flow at current levels or that anticipated operational improvements will be achieved. We may also pursue acquisitions or other strategic priorities that will require additional liquidity beyond the liquidity we generate through our operations. Our cash balance as of September 30, 2023, was $47 million compared to $306 million as of December 31, 2022.

The following table summarizes our cash flows for the periods presented:

	Nine Months Ended September 30,	
(Dollars in millions)	2023	2022
Net cash used in operating activities	$ (310)	$ (246)
Net cash (used in) provided by investing activities	(42)	448
Net cash provided by (used in) financing activities	93	(379)
Effect of exchange rate changes on cash and cash equivalents	—	—
Net decrease in cash and cash equivalents	$ (259)	$ (177)
Free cash flow[1]	$ (335)	$ (262)

(1) Free cash flow is a Non-GAAP measure. The reasons we use this Non-GAAP financial measure and its reconciliation to the most directly comparable U.S. GAAP financial measure is provided above under "—Key Financial and Operating Measures—Non-GAAP Financial Measures."

Operating Activities

Cash usage related to the operating activities increased by $64 million from $246 million for the nine months ended September 30, 2022 to $310 million for the nine months ended September 30, 2023. This was primarily due to cash used to fund working capital for the nine months ended September 30, 2023 when compared to the nine months ended September 30, 2022. The increased working capital was driven by incremental tax payments associated with the R&D capitalization requirements of Section 174 of the Tax Code coupled with incremental investments in inventory and contract assets to combat supply chain lead-times.

Investing Activities

Net cash used in investing activities increased by $490 million for the nine months ended September 30, 2023 when compared to the nine months ended September 30, 2022 primarily due to the prior year investing cash inflow generated from the disposition of our GES and AAC operations.

Financing Activities

Net cash provided by financing activities increased by $472 million for the nine months ended September 30, 2023 compared to the nine months ended September 30, 2022. The increase was primarily related to the dividend of our disposition proceeds to US Holding in the prior year.

Free Cash Flow

Free cash flow usage increased by $73 million to $335 million for nine months ended September 30, 2023 from $262 million for the nine months ended September 30, 2022. This was primarily due to cash used in operating activities noted above for the nine months ended September 30, 2023 when compared to the nine months ended September 30, 2022.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE OF MARKET RISK

Equity Risk

We currently have limited risk related to fluctuations in marketable securities. Outside of pension assets which are disclosed in *Note 12: Pension and Other Postretirement Benefits* to the Consolidated Financial Statements, the only investments the Company holds are overnight money market accounts. Fluctuations are unlikely and would have limited impact on the financial statements of the Company.

Interest Rate Risk

We are exposed to interest rate risk on variable-rate borrowings under our $225 million Term Loan A and our revolving credit facilities under which we had an outstanding balance of $217 million and $110 million, respectively, as of September 30, 2023. A 0.5% increase or decrease in our weighted average interest rate on our variable debt outstanding as of September 30, 2023 would result in an increase or decrease in our annual interest expense of approximately $2 million. The carrying values of the Company’s borrowings under the 2022 Credit Facility approximate their fair values at September 30, 2023. For additional information please refer to *Note 11: Debt*.

Foreign Currency Risk

In certain circumstances, we may be exposed to foreign currency risk. However, as the overwhelming majority of our revenue is derived from U.S. sources directly as a prime contractor or indirectly as a subcontractor for the U.S. government as end-customer, we have limited foreign currency exposure. Currently, our exposure is primarily with the Canadian dollar and limited to receivables owed of $39 million as of September 30, 2023. A 10% fluctuation in exchange rates would not have a material impact on our financial statements. We do not enter into or issue derivative instruments for trading purposes.

Inflation Risk

We have generally been able to anticipate increases in costs when pricing our contracts. Bids for longer-term firm fixed-price contracts typically include assumptions for labor and other cost escalations in amounts that historically have been sufficient to cover cost increases over the period of performance. We have seen impacts due to inflation on isolated programs. These have largely been offset with our internal continuous improvement savings initiatives and improved program performance.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our disclosure controls and procedures as of the end of the quarterly period ended September 30, 2023, as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended. Based on this evaluation, our principal executive officer and principal financial officer has concluded that during the period covered by this report, our disclosure controls and procedures were effective.

Disclosure controls and procedures are designed to ensure that information required to be disclosed by us in our Exchange Act reports is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting that occurred during the quarterly period ended September 30, 2023 covered by this Quarterly Report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

For information relating to legal proceedings, see Note 14 to the unaudited Consolidated Financial Statements in Part 1, Item 1.

ITEM 1A. RISK FACTORS

We are susceptible to a security breach, through cyber-attack, cyber-intrusion, insider threats or otherwise, and to other significant disruptions of our IT networks and related systems, or those of our customers, suppliers, vendors, subcontractors, partners, or other third parties.

We are subject to the risks of cybersecurity incidents described in the section "Risk Factors—We are susceptible to a security breach, through cyber-attack, cyber-intrusion, insider threats or otherwise, and to other significant disruptions of our IT networks and related systems or of those we operate for our customers" in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2022. These risk include that safeguards put in place by third parties, including our customers, subcontractors, suppliers, vendors and partners, may not be effective to minimize the impact of cyber threats, security threats or other business disruptions. From time to time, these third parties have been and continue to be subject to breaches. For example, we are currently taking measures in response to a cyber-attack by a malicious actor impacting one of our suppliers. While this incident has not had a material impact on us at this time, our responses to this and similar incidents may disrupt our business relationships and could negatively affect our operations. Although we have processes designed to assess and confirm certain cybersecurity standards, we are and will remain at risk of a data breach due to the intentional or unintentional non-compliance by a third party's employee or agent or the break-down of a third party's data protection processes, which may not be as sophisticated as ours, or a cyber-attack on a third party's information network or systems. There can be no assurance that cybersecurity incidents at our customers, suppliers, vendors, subcontractors, partners or other third parties will not have a material negative impact on our reputation, business and operations.

Our international business exposes us to additional risks, including risks related to geopolitical and economic factors, laws and regulations.

For the nine months ended September 30, 2023 and 2022, approximately 9% and 8%, respectively, and for the years ended December 31, 2022, 2021, and 2020, approximately 7%, 5% and 8%, respectively, of our revenue was derived from sales to customers located in foreign countries and foreign governments. We cannot assure you that we will maintain significant operations internationally or that any such operations will be successful. International business (including our participation in joint ventures and other joint business arrangements) is subject to numerous political and economic factors, legal requirements, cross-cultural considerations and other risks associated with doing business globally. These risks differ in some respects from those associated with our U.S. business and our exposure to such risks may increase if our international business continues to grow.

Our international business is subject to both U.S. and foreign laws and regulations, which may include, without limitation, laws and regulations relating to import-export controls (such as the ITAR, EAR, and customs laws), tariffs, embargoes, technology transfer restrictions, government contracts and procurement, data privacy and protection, investment, exchange rates and controls, the FCPA and other anti-corruption laws, including the UK Bribery Act and the Canadian Corruption of Foreign Public Officials Act, Article 5 of the Israeli Penal Law of 1977, the anti-boycott provisions under the EAR, U.S. economic sanctions administered by the Office of Foreign Assets Control and other federal agencies, labor and employment, works councils and other labor groups, anti-human trafficking, taxes, environment, immunity, security restrictions and intellectual property. If we or our employees, affiliates, partners or others with whom we work fail to comply with applicable laws and regulations we may be subject to administrative, civil, commercial or criminal penalties and liabilities, including suspension or debarment from government contracts or suspension of our export privileges. Our international business also exposes us to difficulties associated with repatriating cash generated or held abroad in a tax-efficient manner and changes in tax laws. Our customers outside of the U.S. generally have the ability to terminate contracts for default based on performance. Suspension or debarment, or termination of a contract due to default, in particular, could have a material adverse effect on our reputation, our ability to compete for other contracts and our financial position, results of operations and/or cash flows. New regulations and requirements, or changes to existing ones in the various countries in which we operate can significantly increase our costs and risks of doing business internationally. Any such future violations could have a material adverse impact on our reputation, business, results of operations and financial condition.

Changes in laws, regulations, political leadership and environment, or security risks may significantly affect our ability to conduct or continue to conduct business in international markets. Our international business may be impacted by changes in U.S. and foreign national policies and priorities, and geopolitical relationships, any of which may be influenced by changes in the threat environment, political leadership, geopolitical uncertainties, world events, acts of terrorism, bilateral and multi-lateral relationships, government budgets, and economic and political factors more generally, and any of which could impact funding for programs, alter export authorizations, or delay purchasing decisions or customer payments. These changes may affect the defense spending priorities and procurement policies of foreign governments which may affect our international military sales.

The Company is subject to risks associated with a dynamic geopolitical climate, including nation states that could take action to limit our access to key material and subcomponents used in our products. Recently enacted export controls by foreign governments covering rare elements could have a material adverse impact on our business, financial condition and results of operations.

Global economic conditions and fluctuations in foreign currency exchange rates could further impact our business. For example, the tightening of credit in financial markets outside of the U.S. could adversely affect the ability of our customers and suppliers to obtain financing and could result in a decrease in or cancellation of orders for our products and services or impact the ability of our customers to make payments. In addition, the majority of our foreign costs are denominated in local currencies. Over time, an increasing portion of our contracts with paid customers outside of the United States may be denominated in local currencies. Therefore, fluctuations in the value of the U.S. dollar and foreign currencies may affect our results of operations when translated into U.S. dollars. We do not currently engage in currency-hedging activities to limit the risk of exchange rate fluctuations. However, in the future, we may use derivative instruments, such as foreign currency forward and option contracts, to hedge certain exposures to fluctuations in foreign currency exchange rates. The use of such hedging activities may not offset any or more than a portion of the adverse financial effects of unfavorable movements in foreign exchange rates over the limited time the hedges are in place. Moreover, the use of hedging instruments may introduce additional risks if we are unable to structure effective hedges with such instruments.

Our contracts with non-U.S. customers may also include terms and reflect legal requirements that create additional risks including the risk of non-payment or delayed payment by foreign customers and governments. They may include industrial cooperation agreements requiring specific in-country purchases, investments, manufacturing agreements or other operational or financial obligations, including offset obligations, and provide for significant penalties if we fail to meet such requirements. They may also require us to enter into letters of credit, performance or surety bonds, bank guarantees and/or other financial arrangements to secure our performance obligations. We also increasingly are dependent on in-country suppliers and we face risks related to their failure to perform in accordance with the contracts and applicable laws, particularly where we rely on a sole source supplier. Our ability to sell products outside the U.S. could be adversely affected if we are unable to design our products for export on a cost-effective basis or to obtain and retain all necessary export licenses and authorizations on a timely basis.

Conducting business outside of the U.S. also exposes us to the complexity and necessity of using, and disruptions involving, our international dealers, distributors, sales representatives and consultants as well as the difficulties of managing a geographically dispersed organization and culturally diverse workforces, including compliance with applicable U.S. and local laws and practices, such as anti-corruption and anti-trust/competition laws. Contracts with international customers are significantly different than the contracts with our U.S. customers, and some are more complex and require different skills to manage. Our ability to conduct business outside of the U.S. also depends on our ability to attract and retain sufficient qualified personnel with the skills and/or security clearances in the markets in which we do business.

The products and services we provide internationally, including those provided by subsidiaries, subcontractors and joint ventures in which we have an interest, are sometimes in countries with unstable governments, economic or fiscal challenges, military or political conflicts and/or developing legal systems. This may increase the risk to our employees, subcontractors or other third parties, and/or increase the risk of a wide range of liabilities, as well as loss of property or damage to our products.

We are also closely monitoring developments in the war between Israel and Hamas that began on October 7, 2023. At this time, the conflict has the potential to evolve quickly creating uncertainty in the broader Middle East region, along with the potential for disruptions to our Israeli operations in the region including, but not limited to workforce calls for duty, transportation and other logistical impacts and reduced customer confidence.

The occurrence and impact of these factors is difficult to predict, but one or more of them could negatively impact our business, financial condition and results of operations.

As of the date of this Quarterly Report, there have been no other material changes to the risk factors discussed under “Risk Factors” in Part 1, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2022, filed with the SEC on March 28, 2023.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES, USE OF PROCEEDS, AND ISSUER PURCHASES OF EQUITY SECURITIES

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable

ITEM 5. OTHER INFORMATION

(c) Furnish the information required by Item 408(a) of Regulation S-K (17 CFR 229.408(a)).

During the three months ended September 30, 2023, no director or officer of the Company adopted or terminated a “Rule 10b5-1 trading arrangement” or “non Rule 10b5-1 trading arrangement,” as each term is defined in Item 408(a) of Regulation S-K.

ITEM 6. Exhibits

Exhibit Number	Exhibit Description
99.1†	Leonardo DRS, Inc. Incentive-Based Compensation Recoupment Policy, effective October 2, 2023
31.1	Certification by principal executive officer pursuant to Rule 13A-14(a) or 15D-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification by principal financial officer pursuant to Rule 13A-14(a) or 15D-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification by principal executive officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification by principal financial officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS	XBRL Instance Document – the instance document does not appear on the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)

† Identifies each management contract or compensatory plan or arrangement.

SIGNATURES

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

Date: November 2, 2023

LEONARDO DRS, INC.

By: /s/ William J. Lynn III

Name: William J. Lynn III

Title: Chief Executive Officer

Certification of Principal Executive Officer
Pursuant to Exchange Act Rule 13a-14(a)/15d-14(a) as
Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, William J. Lynn III, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the quarter ended September 30, 2023 of Leonardo DRS, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b. Designated such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's third fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 2, 2023

/s/ William J. Lynn III

William J. Lynn III
Chief Executive Officer
(Principal Executive Officer)

Certification of Principal Financial Officer
Pursuant to Exchange Act Rule 13a-14(a)/15d-14(a) as
Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Michael D. Dippold, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the quarter ended September 30, 2023 of Leonardo DRS, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
    a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
    b. Designated such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
    c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
    d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's third fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
    a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
    b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 2, 2023

/s/ Michael D. Dippold

Michael D. Dippold
Chief Financial Officer
(Principal Financial Officer)

Certification of Principal Executive Officer
Pursuant to 18 U.S.C. Section 1350 as
Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Quarterly Report of Leonardo DRS, Inc. (the "Company") on Form 10-Q for the period ended September 30, 2023, as filed with the Securities and Exchange Commission (the "Report"), the undersigned, as the Chief Executive Officer of the Company, hereby certifies pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to his knowledge:

1. The Report, which this statement accompanies, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 2, 2023

/s/ William J. Lynn III

William J. Lynn III
Chief Executive Officer
(Principal Executive Officer)

This written statement accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934.

Certification of Principal Financial Officer
Pursuant to 18 U.S.C. Section 1350 as
Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Quarterly Report of Leonardo DRS, Inc. (the "Company") on Form 10-Q for the period ended September 30, 2023, as filed with the Securities and Exchange Commission (the "Report"), the undersigned, as the Chief Financial Officer of the Company, hereby certifies pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to his knowledge:

1. The Report, which this statement accompanies, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 2, 2023

/s/ Michael D. Dippold

Michael D. Dippold
Chief Financial Officer
(Principal Financial Officer)

This written statement accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934.

Exhibit 99.1

INCENTIVE-BASED COMPENSATION RECOUPMENT POLICY

1.0 SCOPE OF APPLICABILITY

1.1 This policy applies to Leonardo DRS, Inc. businesses and subsidiaries worldwide and applies to its current and former Executive Officers (as defined below).

2.0 PURPOSE

2.1 The purpose of the Leonardo DRS, Inc. Incentive-Based Compensation Recoupment Policy (the “Policy”) is to set forth the circumstances in which Leonardo DRS, Inc. (the “Company”) will recover Erroneously Awarded Compensation (as defined below) received by a current or former Executive Officer (as defined below).

3.0 POLICY

3.1 This Policy applies to all Incentive-Based Compensation received by a current and former Executive Officer: (i) on or after the Effective Date; (ii) after beginning service as an Executive Officer; (iii) who served as an Executive Officer at any time during the performance period for which Incentive-Based Compensation was received; (iv) while the Company has a class of securities listed on a national securities exchange or a national securities association; and (v) during the three completed fiscal years immediately preceding the Required Restatement Date.

3.2 Notwithstanding Paragraph 3.1 above, this Policy applies during any transition period that results from a change in the Company’s fiscal year within or immediately following the three completed fiscal year period. For the avoidance of doubt, any transition period between the last day of the Company’s previous fiscal year-end and the first day of its new fiscal year that comprises a period of nine to 12 months would be deemed a completed fiscal year.

3.3 For the avoidance of doubt, references to Executive Officer throughout this Policy shall be read to refer to current or former Executive Officers in accordance with this Section 3, unless otherwise noted.

4.0 DEFINITIONS

4.1 For purposes of this Policy, the following terms have the definitions set forth below:

4.1.1 **"Accounting Restatement"** shall mean the required revision of a previously issued financial statement for correction of an error in such financial statement that is (i) due to material noncompliance with any applicable financial reporting requirement under the U.S. federal securities laws, including any required accounting restatement to correct an error in a previously issued financial statement that is material to such previously issued financial statement, or (ii) not material to a previously issued financial statement, but would result in a material misstatement if the error were corrected in the current period (i.e., as of the time of the Accounting Restatement) financial statements or left uncorrected in the current period financial statements.

4.1.2 **"Board"** shall mean the Board of Directors of the Company.

4.1.3 **"Committee"** shall mean the Compensation Committee of the Board as constituted from time to time (including any successor committee).

4.1.4 **"Effective Date"** shall mean October 2, 2023.

4.1.5 **"Erroneously Awarded Compensation"** shall mean, with respect to each Executive Officer and in connection with any Accounting Restatement, the amount of Incentive-Based Compensation received by such Executive Officer that exceeds the amount of Incentive-Based Compensation that would have been received by such Executive Officer had it been determined based on the restated amounts set forth in the Accounting Restatement.

4.1.6 **"Executive Officer"** shall mean each individual designated as an "officer" of the Company in accordance with 17 C.F.R. 240.16a-1(f). Identification of an executive officer for purposes of this Policy would include at a minimum executive officers identified pursuant to 17 C.F.R. 229.401(b).

4.1.7 **"Financial Reporting Measures"** means financial measures that are used for evaluating the attainment of Incentive-Based Compensation and that are determined and presented in accordance with the accounting principles used in preparing the Company's financial statements, as well as any financial measures that are derived wholly or in part from such measures. For purposes of this Policy, the Company's stock price and total shareholder return are Financial Reporting Measures. A Financial Reporting Measure need not be presented within the financial statements or included in a filing with the SEC.

4.1.8 **"Incentive-Based Compensation"** means compensation that is granted, earned, or vested based wholly or in part upon the attainment of a Financial Reporting Measure. Incentive Based Compensation is deemed received by an Executive Officer in the Company's fiscal year during which the Financial Reporting Measure specified in the Incentive-Based Compensation award is attained, even if the payment or grant of the Incentive-Based Compensation occurs after the end of that period.

4.1.9 **"Nasdaq"** shall mean the National Association of Securities Dealers Automated Quotations Stock Market.

4.1.10 **"Required Restatement Date"** shall mean the earlier to occur of (i) the date upon which the Board, the Committee, or the officers of the Company authorized to take such action, concludes, or reasonably should have concluded, that the Company is required to prepare an Accounting Restatement, or (ii) the date upon which a court, regulator or other legally authorized body directs the issuer to prepare an Accounting Restatement in a final, non-appealable order or judgment.

4.1.11 **"SEC"** shall mean the U.S. Securities and Exchange Commission.

5.0 RECOVERY OF ERRONEOUSLY AWARDED INCENTIVE-BASED COMPENSATION

5.1 In the event of an Accounting Restatement, the Company shall promptly determine the amount of any Erroneously Awarded Compensation for each Executive Officer in connection with such Accounting Restatement and shall provide written notice to each Executive Officer of (i) the Required Restatement Date, (ii) the amount of Erroneously Awarded Compensation received, and (iii) the method, manner, and time for repayment or return or such Erroneously Awarded Compensation, as applicable. The amount of

Incentive-Based Compensation that is subject to recovery will be computed without regard to any taxes paid.

5.2 The Committee shall have the discretion to reasonably determine the appropriate means of recovery of such Erroneously Awarded Compensation based on applicable facts and circumstances. If an Executive Officer fails to repay Erroneously Awarded Compensation to the Company by the time and in the manner set forth in writing by the Committee, the Company shall take all actions reasonable and appropriate to recover the Erroneously Awarded Compensation from the Executive Officer. The Executive Officer shall be required to reimburse the Company for all expenses, including attorneys' fees, reasonably incurred by the Company in recovering Erroneously Awarded Compensation.

5.3 For Incentive-Based Compensation based on the Company's stock price or total shareholder return, where the amount of Erroneously Awarded Compensation is not subject to mathematical recalculation directly from the information in an Accounting Restatement:

5.3.1 the amount will be based on a reasonable estimate of the effect of the accounting restatement on the Company's stock price or total shareholder return upon which the Incentive-Based Compensation was received; and

5.3.2 the Company will maintain documentation of the determination of that reasonable estimate and provide such documentation to the Nasdaq.

6.0 RECOVERY EXCEPTIONS

6.1 The Company will recover Erroneously Awarded Compensation in accordance with this Policy, except to the extent that any of the following conditions are met and the Committee (provided it is comprised of independent directors at the applicable time), or in the absence of such Committee, a group constituting the majority of the Board's independent directors, has determined that recovery would be impracticable because:

6.1.1 the direct expense reasonably expected to be paid to a third party to assist in enforcing this Policy would exceed the amount to be recovered; provided that before concluding it would be impracticable to recover any amount of

Erroneously Awarded Compensation based on the expense of enforcement, the Company will make a reasonable attempt to recover such Erroneously Awarded Compensation without incurring any third party expense, document such reasonable attempt(s) to recover, and provide such documentation to the Nasdaq;

6.1.2 recovery would violate home country law where that law was adopted prior to November 28, 2022; provided that before concluding that it would be impracticable to recover any amount of Erroneously Awarded Compensation based on violation of home country law, the Company will obtain an opinion of home country counsel, acceptable to the Nasdaq, that recovery would result in such a violation and provide such opinion to the Nasdaq; or

6.1.3 recovery would likely cause an otherwise tax-qualified retirement plan, under which benefits are broadly available to employees of the Company, to fail to meet the requirements of 26 U.S.C. 401(a)(13) or 26 U.S.C. 411(a) and regulations thereunder.

7.0 REPORTING AND DISCLOSURE REQUIREMENTS

7.1 The Company shall file all disclosures with respect to this Policy in accordance with the requirements of the federal securities laws, including the disclosure required by the applicable SEC filings.

8.0 INDEMNIFICATION PROHIBITION

8.1 The Company will not indemnify any current or former Executive Officer against any losses stemming from the application of this Policy to Erroneously Awarded Compensation.

9.0 OTHER RECOUPMENT RIGHTS

9.1 This Policy is not intended to limit the Company’s ability to pursue equitable relief or other means to recover monetary damages resulting from an Executive Officer’s wrongdoing. The Company retains all rights it may have under applicable law.

10.0 APPROVAL, IMPLEMENTATION AND COMPLIANCE

10.1 Administration

10.1.1 The Committee shall have sole discretion in making all determinations under this Policy. Any determinations of the Committee shall be binding on the Executive Officer.

10.2 Amendment

10.2.1 This Policy may be amended from time to time in the Committee's sole discretion.

10.3 Compliance with the Exchange Act

10.3.1 Notwithstanding the foregoing, this Policy shall be interpreted and administered consistent with the applicable securities laws, including the requirements of (i) Section 10D of the Securities Exchange Act of 1934, as amended (the "***Exchange Act***"), as added by Section 954 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, (ii) Rule 10D-1 under the Exchange Act, and (iii) the listing standards adopted by the Nasdaq pursuant to Rule 10D-1, and, to the extent this Policy is in any manner deemed inconsistent with such requirements, this Policy shall be treated as retroactively amended to be compliant with such requirements.

10.4 Saving Clause

10.4.1 To the extent that any of the provisions of this Policy are found by a court of competent jurisdiction to be illegal, invalid, or unenforceable for any reason, such provision shall be deleted, and the balance of this Policy shall not be affected.

11.0 REPORTING SUSPECTED VIOLATION

11.1 DRS Employees are required to immediately report any known or suspected violations of this Policy. Such reports shall be made in a timely manner to any of the following:

- Company Executives, managers, supervisors (who, in turn, must promptly notify one of the following:
- Designated Corporate Counsel;

- DRS General Counsel;
- DRS Alertline https://drs.alertline.com or at 1-800-694-5005, which is available 24 hours a day, 7 days a week. Reports to the Alertline may be made anonymously.