UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

[X] Quarterly Report Pursuant to Section 13 or 15(d)
of the Securities Exchange Act of 1934

For the quarterly period ended: June 30, 2000

[ ] Transition Report Pursuant to Section 13 or 15(d)
of the Securities Exchange Act of 1934

Commission file number: 1-8443

TELOS CORPORATION
(Exact name of registrant as specified in its charter)

Maryland	52-0880974
(State of Incorporation)	(I.R.S. Employer Identification No.)

19886 Ashburn Road, Ashburn, Virginia	20147-2358
(Address of principal executive offices)	(Zip Code)

Registrant's Telephone Number,

including area code: (703) 724-3800

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

As of August 1, 2000, the registrant had 21,241,980 shares of Class A Common Stock, no par value, and 4,037,628 shares of Class B Common Stock, no par value; and 3,185,586 shares of 12% Cumulative Exchangeable Redeemable Preferred Stock par value $.01 per share, outstanding.

No public market exists for the registrant's Common Stock.

Number of pages in this report (excluding exhibits): 24

TELOS CORPORATION AND SUBSIDIARIES

INDEX

PART I. FINANCIAL INFORMATION

PART II. OTHER INFORMATION

PART I - FINANCIAL INFORMATION

TELOS CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

(amounts in thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2000	1999	2000	1999
Sales				
Systems and Support Services	$16,759	$23,068	$32,459	$43,402
Products	15,046	30,876	29,297	47,979
Xacta	3,671	2,196	5,814	3,390
	35,476	56,140	67,570	94,771
Costs and expenses				
Cost of sales	29,402	46,418	57,495	80,594
Selling, general and administrative expenses	4,237	4,073	8,447	8,454
Goodwill amortization	90	132	179	264
Operating income	1,747	5,517	1,449	5,459
Other income (expenses)				
Equity in net losses of Enterworks	--	(5,145)	--	(9,168)
Other income	18	21	38	52
Interest expense	(1,226)	(1,469)	(2,363)	(3,019)
Income(loss) before taxes	539	(1,076)	(876)	(6,676)
Income tax(provision)benefit	(304)	71	183	1,548
Net income (loss)	$ 235	$(1,005)	$ (693)	$(5,128)

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

TELOS CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

(amounts in thousands)

ASSETS

	June 30, 2000	December 31, 1999
Current assets		
Cash and cash equivalents (includes restricted cash of $54 at June 30, 2000 and December 31, 1999)	$ 313	$ 315
Accounts receivable, net	28,114	27,030
Inventories, net	5,008	4,779
Deferred income taxes, current	5,129	4,802
Other current assets	570	83
Total current assets	39,134	37,009
Property and equipment, net of accumulated depreciation of $9,059 and $23,093, respectively	12,307	12,236
Goodwill, net	4,106	4,284
Investment in Enterworks	--	--
Deferred income taxes, long term	2,886	2,930
Other assets	511	427
	$ 58,944	$ 56,886

LIABILITIES AND STOCKHOLDERS' INVESTMENT

	June 30, 2000	December 31, 1999
Current liabilities		
Accounts payable	$ 9,618	$13,792
Other current liabilities	2,533	3,421
Unearned revenue	6,544	5,183
Senior subordinated notes	8,537	--
Accrued compensation and benefits	8,191	7,645
Total current liabilities	35,423	30,041
Senior credit facility	22,069	16,508
Senior subordinated notes	--	8,537
Capital lease obligations	11,190	11,362
Total liabilities	68,682	66,448
Redeemable preferred stock		
Senior redeemable preferred stock	6,266	6,054
Redeemable preferred stock	39,656	36,975
Total preferred stock	45,922	43,029
Stockholders' investment		
Common stock	78	78
Capital in excess of par	--	--
Retained deficit	(55,738)	(52,669)
Total stockholders' investment (deficit)	(55,660)	(52,591)
	$ 58,944	$ 56,886

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

TELOS CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(amounts in thousands)

	Six Months Ended June 30, 2000	Six Months Ended June 30, 1999
Operating activities:		
Net loss	$ (693)	$(5,128)
Adjustments to reconcile net loss to cash (used in) provided by operating activities:		
Gain on sale of fixed assets	--	(88)
Depreciation and amortization	829	2,146
Goodwill amortization	179	264
Other noncash items	344	1,003
Changes in assets and liabilities	(5,098)	14,283
Cash (used in) provided by operating activities	(4,439)	12,480
Investing activities:		
Proceeds from sale of fixed assets	--	171
Investment in capitalized software and other assets	--	(762)
Purchase of property and equipment	(961)	(666)
Cash used in investing activities	(961)	(1,257)
Financing activities:		
Proceeds from (repayment of) borrowings under senior credit facility	5,561	(10,688)
Payments under capital leases	(163)	(191)
Cash provided by (used in) financing activities	5,398	(10,879)
(Decrease) increase in cash and cash equivalents	(2)	344
Cash and cash equivalents at beginning of period	315	408
Cash and cash equivalents at end of period	$ 313	$ 752

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

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. General

The accompanying condensed consolidated financial statements are unaudited and include the accounts of Telos Corporation ("Telos") and its wholly owned subsidiaries (collectively, the "Company"). Significant intercompany transactions have been eliminated. In the opinion of the Company, the accompanying financial statements reflect all adjustments and reclassifications (which include only normal recurring adjustments) necessary for their fair presentation in conformity with generally accepted accounting principles. Interim results are not necessarily indicative of fiscal year performance because of the impact of seasonal and short-term variations. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's annual report on Form 10-K for the fiscal year ended December 31, 1999.

In June 1998, the FASB issued SFAS No. 133, "Accounting or Derivative Instruments and Hedging Activities." SFAS 133 establishes accounting and reporting standards for derivative instruments, including derivative instruments embedded in other contracts, and for hedging activities. SFAS 133, as amended by SFAS 137, "Accounting for Derivative Instruments and Hedging Activities - Deferral of the effective date of SFAS No. 133, an amendment of FASB Statement No. 133" is effective for all quarters of the Company's year ending December 31, 2001. The Company currently does not engage or plan to engage in the use of derivative instruments, and does not expect SFAS 133 to have a material impact on the results of operations.

In June 2000, the FASB issued SFAS 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities" which amends SFAS 133. SFAS 138 amends SFAS 133 to 1)expand the scope of the "normal sales and normal purchases" exception; 2)introduce the benchmark rate as an interest rate that may be hedged; 3)permit a recognized foreign currency denominated asset to be hedged and; 4)allow certain intercompany derivatives that are offset net to be designated as hedging instruments. The Company does not anticipate SFAS 138 to have a material impact on its financial statements.

In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin 101 "Revenue Recognition in Financial Statements" ("SAB101")to provide guidance regarding the recognition, presentation and disclosure of revenue in the financial statements. The Company expects to adopt the provisions of SAB 101 (as amended by SAB 101B which deferred the implementation date by three quarters) on October 1, 2000. Management does not anticipate the adoption of SAB 101 to have a material impact on its results of operations or financial condition.

In April 2000, the FASB issued FASB Interpretation No. 44 "Accounting for Certain Transactions Involving Stock Compensation; Interpretation of APB Opinion No.25" ("FIN 44"). The Company is evaluating the provisions of FIN 44.

Certain reclassifications have been made to the prior year's financial statements to conform to the classifications used in the current period.

Note 2. Deconsolidation of Enterworks, Inc. Subsidiary

On December 30, 1999, Enterworks, Inc. ("Enterworks"), a majority-owned subsidiary of the Company, completed a private placement of 21,739,127 shares of Series A Convertible Preferred Stock ("Preferred Stock") at a price of $1.15 per share. The sale generated gross proceeds of $25,000,000. In addition, the Company entered into a series of concurrent transactions pursuant to which the Company's voting interest in Enterworks was reduced to approximately 34.8%. The concurrent transactions were as follows:

1. The Company converted approximately $7.6 million of its Senior Subordinated Notes, Series B, C and D held by investors, plus the accrued interest and the waiver of prepayment premium associated with these notes, into shares of Enterworks' Common Stock owned by the Company at an exchange ratio of one share of Enterworks' Common Stock for each $1.00 principal amount of notes payable. These subordinated notes had a maturity date of October 1, 2000.

2. Enterworks purchased 5,000,000 shares of Enterworks' Common Stock owned by the Company at a price of $1.00 per share. This amount was reduced by 20% of the Agent's fee, the Company's pro rata share of the proceeds from the transaction. The net amount received was $4.7 million. This transaction, together with the one described above, resulted in an extraordinary gain,

net of tax of $5.3 million, of $8.0 million, which is included in the Company's statement of operations for the year ended December 31, 1999.

3. Enterworks' payable to the Company, which was approximately $24.4 million at December 30, 1999, was cancelled in its entirety before the issuance of Series A Preferred Stock. The forgiveness of the payable increased the Company's investment in Enterworks. Funding required to cover Enterworks' working capital needs from November 30, 1999 to the date of closing was funded by the Company and was repaid through collections from Enterworks' trade accounts receivable. This funding approximated $2.0 million. This forgiveness of intercompany debt is deemed by management to be a normal occurrence of a capital raising transaction.

4. Enterworks issued 4,000,000 shares of Enterworks' Common Stock to Telos concurrent with the issuance of the Enterworks' Series A Preferred Stock. This issuance increased the Company's investment in Enterworks as it increased the number of shares the Company owned in Enterworks.

5. Enterworks issued a warrant to acquire 350,000 shares of Enterworks' Common Stock to Telos' primary lender, Bank of America, in connection with obtaining the necessary approvals for this offering. The exercise price of the warrant equaled $1.15 per share, the same per share price of the Series A Preferred Stock. This warrant was recorded at its fair market value as a charge to interest expense and a reduction to the Company's investment in Enterworks.

6. Telos contributed 210,912 shares of Enterworks' Common Stock owned by Telos to the Enterworks Treasury for the subsequent grant of warrants to the Agent, Deutsche Bank Alex. Brown. This issuance of warrants was also part of the Agent's fee. This contribution of shares was also a charge to interest expense and a reduction to the Company's investment in Enterworks.

As a result of the reduction of the Company's ownership percentage in Enterworks the Company changed its method of accounting for its investment in Enterworks from the consolidation method to the equity method. Pursuant to this change the Company's interest in the losses of Enterworks have been reported separately as "Equity in Net Losses of Enterworks" in the Company's consolidated statement of operations for the six months ended June 30, 2000. Additionally, the Company established an "Investment in Enterworks" account in accordance with APB 18. As of June 30, 2000 and December 31, 1999, respectively, the balance is zero in the Investment in Enterworks account due to the fact that the Company's share of cumulative losses exceeds its investment basis.

Note 3. Sale of Assets

On September 29, 1999, the Company sold substantially all of the assets of its computer maintenance and service business, Telos Field Engineering, Inc. ("TFE"), to TFE Technology Holdings, LLC ("TFE Holdings"), an affiliate of Carr & Company, for $10 million. As a result of this sale, the Company recorded a gain of $4.7 million in its consolidated statement of operations for the year ended December 31, 1999. This gain included a write-off of $2.1 million of goodwill allocated to TFE operations. The Company and TFE Holdings entered into a one-year corporate services agreement on the date of the sale. Under the terms of the Agreement, Telos will continue to provide certain administrative support functions to TFE Holdings, including but not limited to finance and accounting and human resources, in return for a monthly payment.

Note 4. Debt Obligations

Senior Credit Facility

The Company has a $35 million Senior Credit Facility ("Facility") with a bank that matures on July 1, 2001. As of July 1, 2000, the Facility will be classified as a current liability as the Facility will have a term of less than one year. Borrowings under the Facility are collateralized by a majority of the Company's assets including accounts receivable, inventory, and Telos' stock in Enterworks, Inc. The amount of available borrowings fluctuates based on the underlying asset borrowing base.

Senior Subordinated Notes

In 1995 the Company issued Senior Subordinated Notes ("Notes") to certain shareholders. The Notes are classified as either Series B or Series C. Fixed assets of the Company collateralize Series B Notes. Series C Notes are unsecured. Both the Series B and Series C Notes have a maturity date of April 1, 2001 and have interest rates ranging from 14% to 17%. Interest is paid quarterly on January 1, April 1, July 1, and October 1 of each year. The Notes can be prepaid at the Company's option. Additionally, these Notes have a cumulative payment premium of 13.5% per annum payable only upon certain circumstances. These circumstances include an initial public offering of the Company's common stock or a significant refinancing, to the extent that net proceeds from either of the above events are received and are sufficient to pay the premium. Due to the contingent nature of the premium payment, the associated premium expense will only be recorded after the occurrence of a triggering event. At June 30, 2000, the prepayment premium that would be due upon a triggering event is $7.4 million.

In conjunction with the Enterworks private placement offering (Note 2), the Company retired approximately $1.0 million of Series B Notes, and $4.8 million of Series C Notes, in exchange for shares of Enterworks' common stock owned by the Company at an exchange ratio of one share of Enterworks' common stock for each $1.00 principal amount of notes payable. In addition to the retirement of these notes, accrued interest of approximately $300,000 was forgiven and the holders of these notes waived their rights to the prepayment premium associated with these notes.

The balances of the Series B and Series C Notes were $5.5 million and $3.0 million, respectively, at June 30, 2000 and December 31, 1999. At June 30, 2000, the Series B and Series C notes are classified as current liabilities as they have a term of less than one year.

Note 5. Preferred Stock

Senior Redeemable Preferred Stock

The components of the senior redeemable preferred stock are Series A-1 and Series A-2, each with $.01 par value and 1,250 and 1,750 shares authorized, issued and outstanding, respectively. The Series A-1 and Series A-2 carry a cumulative per annum dividend rate of 14.125% of their liquidation value of $1,000 per share. The dividends are payable semi-annually on June 30 and December 31 of each year. The liquidation preference of the senior preferred stock is the face amount of the Series A-1 and A-2 ($1,000 per share), plus all accrued and unpaid dividends. The Company is required to redeem all of the outstanding shares of the stock on December 31, 2001, subject to the legal availability of funds. Mandatory redemptions are required from excess cash flows, as defined in the stock agreements. The Series A-1 and A-2 Preferred Stock is senior to all other present and future equity of the Company. The Series A-1 is senior to the Series A-2. The Company has not declared dividends on its senior redeemable preferred stock since its issuance. At June 30, 2000 and December 31, 1999 cumulative undeclared, unpaid dividends relating to Series A-1 and A-2 redeemable preferred stock totaled $3,266,000 and $3,054,000 respectively.

12% Cumulative Exchangeable Redeemable Preferred Stock

A maximum of 6,000,000 shares of 12% Cumulative Exchangeable Redeemable Preferred Stock (the "Public Preferred Stock"), par value $.01 per share, has been authorized for issuance. The Company initially issued 2,858,723 shares of the Public Preferred Stock pursuant to the acquisition of the Company during fiscal year 1990. The Public Preferred Stock was recorded at fair value on the date of original issue, November 21, 1989, and the Company is making periodic accretions under the interest method of the excess of the redemption value over the recorded value. Accretion for the six months ended June 30, 2000 was $770,000. The Company declared stock dividends totaling 736,863 shares in 1990 and 1991.

In November 1998, the Company retired 410,000 shares of the Public Preferred Stock held by certain shareholders. The Company repurchased the stock at $4.00 per share. The carrying value of these shares was determined to be $3.8 million, and the $2.2 million excess of the carrying amount of these shares of Public Preferred Stock over the redemption price of $1.6 million was recorded as an increase in capital in excess of par; there was no impact on income from this transaction.

The Public Preferred Stock has a 20 year maturity, however, the Company must redeem, out of funds legally available, 20% of the Public Preferred Stock on the 16th 17th, 18th and 19th anniversaries of November 12, 1989, leaving 20% to be redeemed at maturity. On any dividend payment date after November 21, 1991, the Company may exchange the Public Preferred Stock, in whole or in part, for 12% Junior Subordinated Debentures that are redeemable upon terms substantially similar to the Public Preferred Stock and subordinated to all indebtedness for borrowed money and like obligations of the Company.

The Public Preferred Stock accrues a semi-annual dividend at the annual rate of 12% ($1.20) per share, based on the liquidation preference of $10 per share and is fully cumulative. Through November 21, 1995, the Company had the option to pay dividends in additional shares of Preferred Stock in lieu of cash. Dividends in additional shares of the Preferred Stock were paid at the rate of 6% of a share for each $.60 of such dividends not paid in cash. Dividends are payable by the Company, provided the Company has legally available funds under Maryland law, when and if declared by the Board of Directors, commencing June 1, 1990, and on each six month anniversary thereof. For the years 1992 through 1994 and for the dividend payable June 1, 1995, the Company has accrued undeclared dividends in additional shares of preferred stock. These accrued dividends are valued at $3,950,000. Had the Company accrued these dividends on a cash basis, the total amount accrued would have been $15,101,000. For the cash dividends payable since December 1, 1995, the Company has accrued $20,588,000.

The Company has not declared or paid dividends since 1991, due to restrictions and ambiguities relating to the payment of dividends contained within its charter, its working capital facility agreement, and under Maryland law.

Note 6. Reportable Business Segments

The Company adopted SFAS No. 131, "Disclosures About Segments of an Enterprise and Related Information", in 1998 which changes the way the Company reports information about its operating segments. At the beginning of the second quarter 2000, management determined that it evaluates the financial performance of the Company in three reportable operating segments:

Systems and Support Services: provides software development and support services for software including technology insertion, system redesign and software re-engineering. This segment consists of two divisions - solutions and international.

Products: delivers enterprise integration and networking infrastructure solutions to its customers. These solutions include providing commercial hardware, software and services to its customers. This group is capable of staging, installing and deploying large network infrastructures with virtually no disruption to customer's ongoing operations.

Xacta: an emerging e-commerce integrator providing "B2B" trusted e-marketplace solutions to global 2000 companies and emerging digital businesses. Xacta professionals architect, engineer, integrate and support complex "B2B" e-marketplaces and extranets, focusing on security, reliability, scalability and integration with existing systems and processes.

The Company evaluates the performance of its operating segments based on revenue, gross profit and income before goodwill amortization, income taxes, non-recurring items and interest income or expense.

Summarized financial information concerning the Company's reportable segments for the three months ended June 30, 2000 and 1999 is shown in the following table. The "other" column includes corporate related items.

Enterworks, Inc. (Note 2) was disclosed as a segment in 1999 filed reports and therefore it is still identified as a segment in the 1999 captions below.

	Systems and Support Services	Products	Xacta	Enterworks	Other (1)	Total
June 30, 2000						
External Revenues	$16,759	$ 15,046	$ 3,671	$ --	$ --	$35,476
Intersegment Revenues	88	--	--	--	--	88
Gross Profit	2,689	2,055	1,330	--	--	6,074
Segment profit(loss)(3)	1,250	424	163	--	--	1,837
Total assets	11,596	17,375	5,433	--	24,540	58,944
Capital Expenditures	13	219	126	--	211	569
Depreciation & Amortization(2)	$ 111	$ 73	$ 12	$ --	$ 308	$ 504

	Systems and Support Services	Products	Xacta	Enterworks	Other (1)	Total
June 30, 1999						
External Revenues	$23,068	$30,876	$ 2,196	$ --	$ --	$56,140
Intersegment Revenues	--	--	151	--	--	151
Gross Profit	4,181	4,205	1,336	--	--	9,722
Segment profit(loss)(3)	3,137	2,198	314	--	--	5,649
Total assets	26,200	13,766	4,237	6,190	26,402	76,795
Capital Expenditures	10	3	24	133	114	284
Depreciation & Amortization(2)	$ 229	$ 56	$ 8	$ 635	$ 323	$ 1,251

(1) Corporate assets are principally property and equipment, cash and other assets.
(2) Depreciation and amortization includes amounts relating to property and equipment, goodwill, deferred software costs and spare parts inventory.
(3) Segment profit (loss) represents operating income (loss) before goodwill amortization.

The Company does not have material international revenues, profit (loss), assets or capital expenditures. The Company's business is not concentrated in a specific geographical area within the United States, as it has 12 separate facilities located in 4 states and Europe and Asia.

Note 7. Subsequent Event

On July 28, 2000, the Company entered into a Subscription Agreement with certain investors ("Investors"), which provided for the formation of an Oklahoma Limited Liability Company named Telos OK, L.L.C. ("Telos OK"). The Company contributed all of the assets of its Digital Systems Test and Training Simulators ("DSTATS") business as well as its Government Contract with the Department of the Army at Ft. Sill (hereafter referred to as the Company's Ft. Sill business) to Telos OK. The Investors contributed $3.0 million in cash to Telos OK, and at closing Telos OK borrowed $4.0 million cash from a bank. The Company and the Investors have each guaranteed the loan of Telos OK. The Company has guaranteed $2 million and the Investors have guaranteed $1 million. In addition, Telos OK entered into a $500,000 senior credit facility with the same bank, which expires August 1, 2001. Borrowings under the facility, should there be any, will be collateralized by certain assets of Telos OK (primarily accounts receivable). The Company and the Investors have agreed to guarantee this credit facility in the amount of $250,000 each, when and if drawn.

In compliance with the subscription agreement, on the closing date the following consideration was given to the Company for its contribution of assets to Telos OK:

The Company received $6 million in cash, retained $2.5 million in trade receivables of the Ft. Sill and DSTATS businesses, and received a $500,000 receivable from Telos OK for a total consideration of $ 9 million for the contribution of the net assets.

The Company and the Investors on the closing date will each own a 50% voting membership interest in Telos OK, and have signed an operating agreement which provides for three subclasses of membership units, Classes A, B and C. The ownership of these classes is as follows and can change upon Class B redemption:

Class A - owns 20% of Telos OK. The Company and the Investors each own 50% of the 200,000 units of this class. This class has all voting rights of Telos OK and has the sole right to elect the directors of Telos OK. The units in this class do not have redemptive rights.

Class B - owns 40% of Telos OK. The Investors own all 2.9 million units of this class. This class does not have voting rights, but can request the redemption of all or a portion of the units Class B outstanding beginning one year after the closing date, subject to certain restrictions. Class B can redeem no more than 500,000 units per quarter at a price of $1.00 per unit, and such redemption can only be made from the excess cash flow of Telos OK as defined in the agreement.

Class C- owns 40% of Telos OK. The Company owns all 2.9 million units of this class. This class does not have voting rights, and has the same redemptive rights as class B above, except that no right of redemption will exist until all Class B units have been redeemed. In addition, when any of the Class B units have been redeemed, the Company will receive a warrant to purchase a number of Class C units equal to the amount of the Class B units redeemed at a price of $0.01 per unit.

As indicated in the operating agreement, one of the Investors will initially serve as Chairman of the Board and may designate a Secretary, and David Aldrich, President and CEO of the Company, and Thomas Ferrara, Treasurer of the Company, will initially serve in those same capacities for Telos OK. The Company has entered into a corporate services agreement with Telos OK whereby the Company will provide certain administrative support functions to Telos OK, including but not limited to finance and accounting and human resources, in return for a monthly payment.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

The following unaudited Pro Forma Consolidated Balance Sheet as of June 30, 2000 presents the pro forma impact of the transaction as if it occurred on June 30, 2000. The unaudited Pro Forma Consolidated Statements of Operations for the year ended December 31, 1999 and for the six months ended June 30, 2000 ("pro forma financial information") present the pro forma effect of the transaction as if it occurred as of January 1, 1999.

The objective of pro forma financial information is to provide investors with information about the estimated continuing impact of particular completed or probable transactions by indicating how the transactions might have affected historical financial statements had they occurred at an earlier date.

TELOS CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

TELOS CORPORATION AND SUBSIDIARIES

PRO FORMA CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE SIX MONTHS ENDED JUNE 30, 2000

(Unaudited)

(amounts in thousands)

	Form 10-Q Balances	Elimination of Operations of Telos OK	Adjustments	Pro Forma Balances
Sales				
Systems and Support Services	$32,459	$(11,565)(d)	$ --	$20,894
Products	29,297	--	--	29,297
Xacta	5,814	--	--	5,814
	67,570	(11,565)	--	56,005
Costs and expenses				
Cost of sales	57,495	(9,558)(d)	--	47,937
Selling, general and administrative expenses	8,447	--	--	8,447
Goodwill amortization	179	--	--	179
Operating income (loss)	1,449	(2,007)	--	(558)
Other income (expenses)				
Equity in net losses of Enterworks	--	--	--	--
Equity in earnings of Telos OK	--	--	1,004 (e)	1,004
Other income	38	--	--	38
Interest expense	(2,363)	--	--	(2,363)
(Loss) income before taxes	(876)	(2,007)	1,004	(1,879)
Income tax benefit	183	--	459 (f)	642
Net (loss)income	$ (693)	$(2,007)	$ 1,463	$(1,237)

Please see Notes to the unaudited Pro Forma Consolidated Statement of Operations and Consolidated Balance Sheet.

TELOS CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

TELOS CORPORATION AND SUBSIDIARIES

PRO FORMA CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE YEAR ENDED DECEMBER 31, 1999

(Unaudited)

(amounts in thousands)

	Form 10-K Balances	Elimination of Operations of Telos OK	Adjustments	Pro Forma Balances
Sales				
Systems and Support Services	$93,538	$(19,614)(d)	$ --	$73,924
Products	77,826	--	--	77,826
Enterworks	--	--	--	--
	171,364	(19,614)	--	151,750
Costs and expenses				
Cost of sales	151,216	(17,806)(d)	--	133,410
Selling, general and administrative expenses	17,459	--	--	17,459
Goodwill amortization	489	--	--	489
Operating income (loss)	2,200	(1,808)	--	392
Other income (expenses)				
Equity in net losses of Enterworks	(18,765)	--	--	(18,765)
Equity in earnings of Telos OK	--	--	904 (e)	904
Other income	67	--	--	67
Gain on sale of assets	4,731	--	--	4,731
Interest expense	(6,065)	--	--	(6,065)
(Loss) income before taxes	(17,832)	(1,808)	904	(18,736)
Income tax benefit	7,853	--	404 (f)	8,257
(Loss) income before extraordinary item	(9,979)	(1,808)	1,308	(10,479)
Extraordinary item	8,015	--	--	8,015
Net (loss)income	$ (1,964)	$(1,808)	$ 1,308	$(2,464)

Please see Notes to the unaudited Pro Forma Consolidated Statement of Operations and Consolidated Balance Sheet.

TELOS CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

TELOS CORPORATION AND SUBSIDIARIES

PRO FORMA CONDENSED CONSOLIDATED BALANCE SHEET

AT JUNE 30, 2000

(Unaudited)

(amounts in thousands)

ASSETS

	Form 10-Q Balances	Adjustments and Contribution to Telos OK	Adjustments	Pro Forma Balances
Current assets				
Cash and cash equivalents	$ 313	$6,500(a)	$ (500)(g)	$ 6,313
Accounts receivable, net	28,114	(1,322)b)	--	26,792
Inventories, net	5,008	--	--	5,008
Deferred income taxes, current	5,129	--	367(f)	5,496
Other current assets	570	(31)(b)	500(g)	1,039
Total current assets	39,134	5,147	367	44,648
Property and equipment, net	12,307	(50)(b)	--	12,257
Goodwill, net	4,106	(1,232)(b)	--	2,874
Investment in Enterworks	--	--	--	--
Investment in Telos OK	--	--	--	--
Deferred income taxes, long term	2,886	--	--	2,886
Other assets	511	--	--	511
	$58,944	$3,865	$ 367	$63,176

LIABILITIES AND STOCKHOLDERS' INVESTMENT

	Form 10-Q Balances	Adjustments and Contribution to Telos OK	Adjustments	Pro Forma Balances
Current liabilities				
Accounts payable	$ 9,618	$ (216)(b)	$ --	$ 9,402
Other current liabilities	2,533	(16)(b)	(92)(f)	2,425
Unearned revenue	6,544	--	--	6,544
Senior subordinated notes	8,537	--	--	8,537
Accrued compensation and benefits	8,191	(1,873)(b)	--	6,318
Total current liabilities	35,423	(2,105)	(92)	33,226
Senior credit facility	22,069	--	--	22,069
Capital lease obligations	11,190	--	--	11,190
Total liabilities	68,682	(2,105)	(92)	66,485
Redeemable preferred stock				
Senior redeemable preferred stock	6,266	--	--	6,266
Redeemable preferred stock	39,656	--	--	39,656
Total preferred stock	45,922	--	--	45,922
Stockholders' investment				
Common stock	78	--	--	78
Capital in excess of par	--	5,970 (c)	--	5,970
Retained deficit	(55,738)	--	459(f)	(55,279)
Total stockholders' investment	(55,660)	5,970	459	(49,231)
	$ 58,944	$3,865	$ 367	$63,176

Please see Notes to the unaudited Pro Forma Consolidated Statement of Operations and Consolidated Balance Sheet.

Pro Forma Adjustments

The pro forma adjustments outlined below present adjustments related to the transaction:

a) Reflects the net receipt of $6.0 million from Telos OK in connection with the subscription agreement. The Company received $7.0 million less $1.0 million retained in the business of Telos OK.

b) Reflects the elimination of the June 30, 2000 FT. Sill and DSTATS businesses' accounts from the Company's balance sheet. These net assets consist of the following:

	(in thousands)
Accounts receivable	$ 1,322
Property and equipment, net	50
Other current assets	31
Goodwill	1,232
Accounts payable	(216)
Accrued expenses	(1,889)
	$ 530

c) Reflects the $6.0 million excess of the cash received over the net assets contributed. There is no impact on income from this transaction.

d) Reflects the adjustment to the Statements of Operations for the six month period ended June 30, 2000 and the year ended December 31, 1999 to separate the operations of the Ft. Sill and DSTATS businesses from the respective periods.

e) Reflects the Company's 50% interest in the net income of Telos OK for the six months ended June 30, 2000 and the year ended December 31, 1999.

f) Reflects the changes to the income tax provision and corresponding deferred tax assets and liabilities in order to present a stand-alone income tax provision for the Company in accordance with SFAS 109 for the six months ended June 30, 2000 and for the year ended December 31, 1999.

g) Reflects additional $500,000 to be received from Telos OK at a future date for the Company's contribution of receivables.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

General

Sales for the first six months of 2000 were $67.6 million, a decrease of $27.2 million or 28.7% as compared to the same 1999 period. This decrease was primarily attributable to a $18.7 million decrease in sales from the Company's Products Group which experienced decreased sales from its Joint Recruitive Information Support Services Blanket Purchase Agreement. This decrease is also attributable to the sale of the Company's Field Engineering division ("TFE") in September 1999.

Operating income through the first six months of 2000 was $1.4 million as compared to operating income of $5.5 million during the same 1999 period. Operating profitability declined principally as a result of the sale of TFE and the decline in sales in the Products Group as discussed above.

Total backlog from existing contracts was approximately $237.2 million and $242.2 million as of June 30, 2000 and December 31, 1999, respectively. As of June 30, 2000, the funded backlog of the Company totaled $56.9 million, an increase of $12.2 million from December 31, 1999. Funded backlog represents aggregate contract revenues remaining to be earned by the Company at a given time, but only to the extent, in the case of government contracts, funded by a procuring government agency and allotted to the contracts.

Results of Operations

The condensed consolidated statements of operations include the results of operations of Telos Corporation and its wholly owned subsidiaries. The major elements of the Company's operating expenses as a percentage of sales for the three and six month periods ended June 30, 2000 and 1999 are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2000	1999	2000	1999
Sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	82.9	82.7	85.1	85.0
SG&A expenses	11.9	7.3	12.5	8.9
Goodwill amortization	0.3	0.2	0.3	0.3
Operating income	4.9	9.8	2.1	5.8
Other income	0.1	--	0.1	0.1
Equity in net losses of Enterworks	--	(9.1)	--	(9.7)
Interest expense	(3.4)	(2.6)	(3.5)	(3.2)
Income tax(provision) benefit	(0.9)	0.1	0.3	1.6
Net income (loss)	0.7%	(1.8)%	(1.0)%	(5.4)%

Financial Data by Market Segment

Sales, gross profit, and gross margin by market segment for the periods designated below are as follows:

	Three Months Ended June 30, 2000	Three Months Ended June 30, 1999	Six Months Ended June 30, 2000	Six Months Ended June 30, 1999
	(amounts in thousands)			
Sales:				
Systems and Support Services	$ 16,759	$ 23,068	$ 32,459	$ 43,402
Products	15,046	30,876	29,297	47,979
Xacta	3,671	2,196	5,814	3,390
Total	$ 35,476	$ 56,140	$ 67,570	$ 94,771
Gross Profit:				
Systems and Support Services	$ 2,689	$ 4,181	$ 4,725	$ 7,562
Products	2,055	4,205	3,423	5,134
Xacta	1,330	1,336	1,927	1,481
Total	$ 6,074	$ 9,722	$ 10,075	$ 14,177
Gross Margin:				
Systems and Support Services	16.1%	18.1%	14.6%	17.4%
Products	13.7%	13.6%	11.7%	10.7%
Xacta	36.2%	60.9%	33.2%	43.7%
Total	17.1%	17.3%	14.9%	15.0%

For the three month period ended June 30, 2000, sales decreased by $20.7 million, or 36.8% to $35.5 million from $56.1 million for the comparable 1999 period. Of the $20.7 million decrease, $15.8 million was attributable to the Products Group, which experienced decreased sales from its Joint Recruitive Information Support Services Blanket Purchase Agreement ("JRISS BPA"). The decrease in sales was also attributable to the Systems and Support Services Group, which experienced a decline of $6.3 million in sales for the three month period ended June 30, 2000 compared to the same period in 1999. This decline is mostly due to the sale of TFE in September 1999. TFE sales were $8.6 million for the second quarter of 1999. Offsetting these decreases was an increase in Xacta revenue of $1.5 million from second quarter 2000 compared to second quarter 1999. This increase is primarily due to increased sales in the Company's information security product line.

Sales decreased $27.2 million or 28.7% to $67.6 million for the six months ended June 30, 2000, from $94.8 million for the comparable 1999 period. The decrease for the six month period includes an $18.7 million decrease in Product sales, a decrease of $10.9 million in Systems and Support Services revenue, partially offset by a $2.4 million increase in sales in its Xacta group. This decrease in the six month revenue is primarily due to the decrease in revenue from the JRISS BPA as well as the sale of TFE. These decreases were slightly offset by increased sales under the Information Security product line of $2.0 million.

Cost of sales was 82.9% of sales for the quarter and 85.1% of sales for the six months ended June 30, 2000, as compared to 82.7% and 85.0% for the same periods in 1999. The slight increases in cost of sales as a percentage of sales are primarily attributable to a one-time high margin transaction with one of the Company's partners recorded in the second quarter of 1999.

Gross profit decreased $3.6 million in the three-month period to $6.1 million in 2000, from $9.7 million in the comparable 1999 period. In the six month period, gross profit decreased $4.1 million to $10.1 million from $14.2 million in 1999. These declines are mostly attributable to the decreases in sales volume discussed above. Gross margins were 17.1% and 14.9%, respectively, for the three and six month periods of 2000 as compared to 17.3% and 15.0%, respectively, for the comparable periods of 1999.

Selling, general, and administrative expense ("SG&A")increased by approximately $164,000 or 4.0%, to $4.2 million in the second quarter of 2000 from $4.1 million in the comparable period of 1999. For the six-month period of 2000, SG&A remained at $8.4 million compared to the same period in 1999.

SG&A as a percentage of revenues increased to 11.9% for the second quarter of 2000 from 7.3% in the comparable 1999 period. SG&A as a percentage of revenues for the six-month period ended June 30, 2000 increased to 12.5% from 8.9% compared to the same period in 1999.

Goodwill amortization expense decreased $42,000 for the comparative three-month periods of 2000 and 1999, and decreased by $85,000 to $179,000 for the six months ended June 30, 2000 compared to the same period in 1999. The reductions are due to a write off of the goodwill balance associated with the sale of TFE in September 1999.

Operating income decreased by $3.8 million to $1.7 million in the three month period ended June 30, 2000 from $5.5 million of operating profit in the comparable 1999 period. Operating income decreased $4.0 million to $1.5 million for the six months ended June 30, 2000 from $5.5 million for the six month period ended June 30, 1999. These decreases in operating profit for the three and six-month periods are mostly attributable to the decrease in gross profit.

Interest expense decreased approximately $200,000 to $1.2 million in the second quarter of 2000 from $1.4 million in the comparable 1999 period, and decreased approximately $700,000 to $2.3 million for the six months ended June 30, 2000 from $3.0 million for the comparable 1999 period. These decreases are due to decreased debt levels in 2000.

The Company recorded an income tax provision for the three months ended June 30, 2000 of approximately $300,000. This tax provision was primarily attributable to provisions for state income taxes. The income tax benefit was $183,000 for the six months ended June 30, 2000. This tax benefit was principally due to the net operating loss carryforwards generated by the Company. The Company's net deferred tax asset includes substantial amounts of net operating loss carryforwards. Failure to achieve forecasted taxable income may affect the ultimate realization of the net deferred tax assets. Management believes the Company will generate taxable income in excess of operating losses sufficient in amounts to realize the net deferred tax assets. The Company has a valuation allowance of approximately $600,000 for primarily state net operating losses it does not believe it will realize. The Company recorded income tax benefits of $71,000 and $1.5 million for the three and six months ended June 30, 1999, respectively. These tax benefits were also due to net operating loss carryforwards generated during the first quarter of 1999.

Liquidity and Capital Resources

For the six months ended June 30, 2000, the Company used $4.4 million of cash in its operating activities. This cash was used to reduce the Company's accounts payable balance by $4.2 million and fund losses incurred in operations. Cash used in investing activities was approximately $1.0 million. Cash was provided by financing activities during the quarter under borrowings under the Company's credit facility of $5.6 million.

At June 30, 2000, the Company had outstanding debt and long term obligations of $41.8 million, consisting of $22.1 million under the secured senior credit facility, $8.5 million in subordinated debt, and $11.2 million in capital lease obligations. The Company believes it will generate enough funds in the ordinary course of business during the next twelve months to fund its operations and service its debt and capital lease obligations.

At June 30, 2000, the Company had an outstanding balance of $22.1 million on its $35 million Senior Credit Facility (the "Facility"). The Facility matures on July 1, 2001 and is collateralized by a majority of the Company's assets (including inventory, accounts receivable and Telos' stock in Enterworks). The amount of borrowings fluctuates based on the underlying asset borrowing base as well as the Company's working capital requirements. The Facility has various covenants that may, among other things, restrict the ability of the Company to merge with another entity, sell or transfer certain assets, pay dividends and make other distributions beyond certain limitations. The Facility also requires the Company to meet certain leverage, net worth, interest coverage and operating goals.

New Accounting Pronouncements

In June 1998, the Financial Accounting Standards Board ("FASB") issued SFAS No. 133, "Accounting or Derivative Instruments and Hedging Activities." SFAS 133 establishes accounting and reporting standards for derivative instruments, including derivative instruments embedded in other contracts, and for hedging activities. SFAS 133, as amended by SFAS 137, "Accounting for Derivative Instruments and Hedging Activities - Deferral of the effective date of FASB Statement No. 133, an amendment of FASB Statement No. 133" is effective for all quarters of the Company's year ending December 31, 2001. The Company currently does not engage or plan to engage in the use of derivative instruments, and does not expect SFAS 133 to have a material impact on the results of operations.

In June 2000, the FASB issued SFAS 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities" which amends SFAS 133. SFAS 138 amends SFAS 133 to 1) expand the scope of the "normal sales and normal purchases" exception; 2) introduce the benchmark rate as an interest rate that may be hedged; 3) permit a recognized foreign currency denominated asset to be hedged and; 4) allow certain intercompany derivatives that are offset net to be designated as hedging instruments. The Company does not anticipate SFAS 138 to have a material impact on its financial statements.

In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin 101 "Revenue Recognition in Financial Statements" ("SAB 101") to provide guidance regarding the recognition, presentation and disclosure of revenue in the financial statements. The Company expects to adopt the provisions of SAB 101 (as amended by SAB 101B which deferred the implementation date by three quarters) on October 1, 2000. Management does not anticipate the adoption of SAB 101 to have a material impact on its results of operations or financial condition.

In April 2000, the FASB issued FASB Interpretation No. 44 "Accounting for Certain Transactions Involving Stock Compensation; Interpretation of APB Opinion No.25" ("FIN 44"). The Company is evaluating the provisions of FIN 44.

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains forward-looking statements. For this purpose, any statements contained herein that are not statements of historical fact may be deemed to be forward-looking statements. Without limiting the foregoing, the words "believes," "anticipates," "plans," "expects" and similar expressions are intended to identify forward-looking statements. There are a number of important factors that could cause the Company's actual results to differ materially from those indicated by such forward-looking statements. These factors include, without limitation, those set forth below under the caption "Certain Factors That May Affect Future Results."

Certain Factors That May Affect Future Results

The following important factors, among others, could cause actual results to differ materially from those indicated by forward-looking statements made in this Quarterly Report on Form 10-Q and presented elsewhere by management from time to time.

A number of uncertainties exist that could affect the Company's future operating results, including, without limitation, general economic conditions, the timing and approval of the federal government's fiscal year budget, business growth through obtaining new business and, once obtained, the Company's ability to successfully perform at a profit, the Company's ability to convert contract backlog to revenue, the Company's ability to secure adequate capital and financing to support continued business growth, and the risk of the Federal government terminating contracts with the Company. While the Company has not experienced contract terminations with the Federal government, the Federal government can terminate at its convenience. Should this occur, the Company's operating results could be adversely impacted.

As a high percentage of the Company's revenue is derived from business with the federal government, the Company's operating results could be adversely impacted should the Federal government not approve and implement its annual budget in a timely fashion.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The Company's exposure to market risk for changes in interest rates relates primarily to the Company's long-term debt obligations.

The Company is exposed to interest rate volatility with regard to its variable rate debt obligations under its Senior Credit Facility. This facility bears interest at 1.00%, subject to certain adjustments, over the bank's base rate. The weighted average interest rate for the first six months of 2000 was 9.86%. This facility expires on July 1, 2001 and has outstanding balance of $22.1 million at June 30, 2000.

The Company's other long-term debt at June 30, 2000 consists of Senior Subordinated Notes B, and C, which bear interest at fixed rates ranging from 14% to 17%. The Senior Subordinated Notes mature as to principal in the aggregate amount of $8,537,000 on April 1, 2001. The Company has no cash flow exposure due to rate changes for its Senior Subordinated Notes.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

The Company is party to various lawsuits arising in the ordinary course of business. In the opinion of management, while the results of litigation cannot be predicted with certainty, the final outcome of such matters will not have a material adverse effect on the Company's consolidated financial position, results of operations, or of cash flows.

Item 3. Defaults Upon Senior Securities

Senior Redeemable Preferred Stock

The Company has not declared dividends on its Senior Redeemable Preferred Stock, Series A-1 and A-2, since its issuance. Total undeclared unpaid dividends accrued for financial reporting purposes are $3.3 million for the Series A-1 and A-2 Preferred Stock at June 30, 2000.

12% Cumulative Exchangeable Redeemable Preferred Stock

Through November 21, 1995, the Company had the option to pay dividends in additional shares of Preferred Stock in lieu of cash (provided there were no blocks on payment as further discussed below). Dividends are payable by the Company, provided the Company has legally available funds under Maryland law and is able to pay dividends under its charter and other corporate documents, when and if declared by the Board of Directors, commencing June 1, 1990, and on each six month anniversary thereof. Dividends in additional shares of the Preferred Stock were paid at the rate of 6% of a share for each $.60 of such dividends not paid in cash. Cumulative undeclared dividends as of June 30, 2000 accrued for financial reporting purposes totaled $24.5 million. Dividends for the years 1992 through 1994 and for the dividend payable June 1, 1995 were accrued under the assumption that the dividend will be paid in additional shares of preferred stock and are valued at $3,950,000. Had the Company accrued these dividends on a cash basis, the total amount accrued would have been $15,101,000. For the cash dividends payable since December 1, 1995 the Company has accrued $20,588,000.

The Company has not declared or paid dividends since 1991, due to restrictions and ambiguities relating to the payment of dividends contained within its charter, its working capital facility agreement, and under Maryland law.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits:

27 Financial Data Schedule

(b) Reports on Form 8-K: None.

Items 2, 4, and 5 are not applicable and have been omitted.

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: Telos Corporation

August 14, 2000

/s/ Thomas J. Ferrara

Thomas J. Ferrara
(Principal Financial Officer &
Principal Accounting Officer)

5

This schedule contains summary financial information extracted from the consolidated balance sheets and statements of operations for Telos Corporation and is qualified in its entirety by reference to such financial statements.

0000320121
Telos Corporation
U.S. Dollars

6-MOS
DEC-31-2000
JAN-01-2000
JUN-30-2000
1
313,000
0
29,138,000
1,024,000
5,008,000
39,134,000
21,366,000
9,059,000
58,944,000
35,423,000
22,069,000
45,922,000
0
78,000
(55,738,000)
58,944,000
67,570,000
67,570,000
57,495,000
57,495,000
0
194,000
2,363,000
(876,000)
(183,000)
(693,000)
0
0
0
(693,000)
0
0