

Deferred tax assets	711	208
Intangible assets, net	1,293	2,836
Other assets	2,724	2,777
Assets of business transferred under contractual arrangements	779	1,124
	-----	-----
Total assets	\$ 35,787	\$ 47,248
	=====	=====

Liabilities and Stockholders' Investment

Current liabilities:

Current portion of long-term debt	\$ 0	\$ 1,333
Accounts payable and other current liabilities	6,596	12,063
Accrued expenses	6,510	5,935
Dividends payable	76	77
Net liabilities of business transferred under contractual arrangements	0	6,747
	-----	-----
Total current liabilities	13,182	26,155

Long-term debt	6,338	5,370
Deferred compensation	1,736	1,871
	-----	-----
Total liabilities	21,256	33,396
	-----	-----

Commitments and contingencies

Stockholders' investment:

Common stock, par value \$.05 per share, authorized 5,000,000 shares; issued 2,187,217 shares in 1999 and 2,186,905 in 1998	109	109
Paid-in surplus	3,835	3,832
Retained earnings	11,379	10,703
Treasury stock, at cost (72,000 shares in 1999 and 1998)	(792)	(792)
	-----	-----
Total stockholders' investment	14,531	13,852
	-----	-----
Total liabilities and stockholders' investment	\$ 35,787	\$ 47,248
	=====	=====

</TABLE>

<TABLE>

VSE Corporation and Subsidiaries
Consolidated Financial Statements (Unaudited)

Consolidated Statements of Income For the three and nine months ended September 30,

(in thousands, except share amounts)

<CAPTION>

	1999		1998	
	Three Months	Nine Months	Three Months	Nine Months
	-----	-----	-----	-----
<S>	<C>	<C>	<C>	<C>
Revenues, principally from contracts	\$ 36,609	\$ 122,848	\$ 44,203	\$ 123,419
Costs and expenses of contracts	35,385	119,364	42,759	119,464
	-----	-----	-----	-----
Gross profit	1,224	3,484	1,444	3,955
Selling, general and administrative expenses	36	528	183	479
Loss on CMstat operations	0	1,499	307	1,815
Interest expense	64	91	42	57
	-----	-----	-----	-----
Pretax income	1,124	1,366	912	1,604

Provision for income taxes . . .	449	462	239	564
Net income	\$ 675	\$ 904	\$ 673	\$ 1,040

Basic earnings per share:

Net income	\$ 0.32	\$ 0.43	\$ 0.32	\$ 0.49
----------------------	---------	---------	---------	---------

Diluted earnings per share:

Net income	\$ 0.32	\$ 0.43	\$ 0.32	\$ 0.49
----------------------	---------	---------	---------	---------

Weighted average shares

outstanding:	2,115,061	2,114,967	2,122,517	2,128,002
--------------	-----------	-----------	-----------	-----------

</TABLE>

<TABLE>

VSE Corporation and Subsidiaries
Consolidated Financial Statements (Unaudited)

Consolidated Statements of Stockholders' Investment

(in thousands)

<CAPTION>

	Common Stock Shares	Paid-In Amount	Retained Surplus	Retained Earnings	Treasury Stock	ESOP Obligation
Balance at December 31, 1997 . .	2,165	\$ 108	\$ 3,631	\$ 9,422	\$ --	\$ (680)
Net income for the year	--	--	1,595	--	--	--
ESOP Obligation	--	--	--	--	--	(112)
Purchase of Treasury Stock	--	--	--	(792)	792	--
Issuance of stock . . .	22	1	201	--	--	--
Dividends declared (\$.144)	--	--	(314)	--	--	--
Balance at December 31, 1998 . .	2,187	109	3,832	10,703	(792)	0
Net income for the period . . .	--	--	904	--	--	--
Issuance of stock . . .	--	--	3	--	--	--
Dividends declared (\$.108)	--	--	(228)	--	--	--
Balance at September 30, 1999 . .	2,187	\$ 109	\$ 3,835	\$ 11,379	\$ (792)	\$ 0

</TABLE>

<TABLE>

VSE Corporation and Subsidiaries
Consolidated Financial Statements (Unaudited)

Consolidated Statements of Cash Flows For the nine months ended September 30,

(in thousands)

<CAPTION>

	1999	1998
	-----	-----
<S>	<C>	<C>
Cash flows from operating activities:		
Net income	\$ 904	\$ 1,040
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,277	1,150
Deferred compensation plan expense	34	109
Change in assets and liabilities (Increase) decrease in:		
Accounts receivable	11,154	(4,891)
Other current assets and noncurrent assets	1,223	(729)
Deferred taxes, net	(980)	(103)
Increase (decrease) in:		
Accounts payable and other current liabilities	(5,453)	5,021
Accrued expenses	575	1,137
Net liabilities of business transferred under contractual arrangements	(6,744)	1,153
	-----	-----
Net cash provided by operating activities	1,990	3,887
Cash flows from investing activities:		
Purchase of property and equipment, (net of dispositions)	(977)	(524)
Net (payments of) proceeds from deferred compensation	(183)	119
	-----	-----
Net cash used in investing activities	(1,160)	(405)
Cash flows from financing activities:		
Net payments of bank loan	(365)	(3,068)
Stock grants	3	202
Advance to ESOP	0	(112)
Cash dividends paid	(229)	(236)
	-----	-----
Net cash used in financing activities	(591)	(3,214)
	-----	-----
Net increase in cash and cash equivalents	239	268
Cash and cash equivalents at beginning of period	49	15
	-----	-----
Cash and cash equivalents at end of period	\$ 288	\$ 283
	=====	=====

</TABLE>

VSE CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the nine month period ended September 30, 1999 are not necessarily indicative of the results that may be expected for the year ending December 31, 1999. For further information refer to the consolidated financial statements and footnotes thereto included in the VSE Corporation Annual Report on Form 10-K for the year ended December 31, 1998.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Debt

VSE has a loan agreement with a syndicate of banks that included a revolving loan and a term loan. The original principal amount of the term loan was \$4 million and the term of the loan was four years. There were no principal payments due during the first 12 months of the loan. Monthly principal payments of approximately \$111 thousand were due in 36 installments beginning August 1998 through July 2001. During September 1999, VSE repaid the principal amount in full, and the term loan portion of the loan agreement no longer exists. Repayment of the term loan did not cause any changes in the terms related to the revolving loan portion of the agreement.

Litigation

The company and its subsidiaries have, in the normal course of business, certain other claims against them and against other parties. In the opinion of management, the resolution of these claims will not have a material adverse effect on the company's results of operations or financial position.

VSE CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Segment Information

Prior to May 21, 1999, VSE had two reportable segments: the engineering, logistics, management, and technical services segment ("ELMTS"), which provides diversified engineering, technical, and management services principally to agencies of the United States Government and to other government prime contractors; and the software products and services segment ("SPS"), which provides application software and services related to the installation of the software to primarily commercial customers.

On May 21, 1999, the company sold all of its interests in the SPS segment for an \$800 thousand promissory note and certain fixed assets valued at approximately \$342 thousand. The sale is a divestiture for legal and tax purposes but not for accounting purposes. The sale is not afforded treatment of a discontinued operation for accounting purposes under Staff Accounting Bulletin No. 30 "Accounting for Divestiture of a Subsidiary or Other Business Operation" ("SAB No. 30") since the sale did not transfer the risks of ownership as it is interpreted under SAB No. 30, because the sales price is primarily dependent on the buyer's ability to repay the promissory note.

As such, the results of the SPS segment will be included in the company's financial statements and are presented as the single line item "Loss on CMstat operations" in the Consolidated Statement of Operations. The assets and liabilities are presented as separate line items in the Consolidated Balance Sheet as "Assets of business transferred under contractual arrangements" and "Net liabilities of business transferred under contractual arrangements", respectively.

<TABLE>

The following table presents revenues and other financial information by business segment for the three and nine month periods ended September 30, 1999, and September 30, 1998, in thousands:

<CAPTION>

Three months ended September 30, 1999	ELMTS	SPS	Total
-----	-----	-----	-----
<S>	<C>	<C>	<C>

Revenues from unaffiliated customers	\$ 36,609	\$ 0	\$ 36,609
Interest expense	64	0	64
Depreciation and amortization	433	0	433
Operating income	1,124	0	1,124
Expenditures for capital assets	339	0	339

VSE CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Nine months ended September 30, 1999	ELMTS	SPS	Total

<S>	<C>	<C>	<C>
Revenues from unaffiliated customers	\$122,848	\$ 902	\$123,750
Interest expense	91	128	219
Depreciation and amortization	1,277	105	1,382
Operating income (loss)	2,844	(1,478)	1,366
Expenditures for capital assets	1,158	25	1,183

Three months ended September 30, 1998	ELMTS	SPS	Total

<S>	<C>	<C>	<C>
Revenues from unaffiliated customers	\$ 44,203	\$ 880	\$ 45,083
Interest expense	42	133	175
Depreciation and amortization	391	64	455
Operating income (loss)	1,197	(285)	912
Expenditures for capital assets	315	4	319

Nine months ended September 30, 1998	ELMTS	SPS	Total

<S>	<C>	<C>	<C>
Revenues from unaffiliated customers	\$123,419	\$2,358	\$125,777
Interest expense	57	370	427
Depreciation and amortization	1,150	185	1,335
Operating income (loss)	3,316	(1,712)	1,604
Expenditures for capital assets	537	37	574

</TABLE>

VSE CORPORATION AND SUBSIDIARIES
Management Discussion and Analysis

VSE and its subsidiaries and divisions have two reportable segments: the engineering, logistics, management and technical services segment ("ELMTS") and the software products and services segment ("SPS").

Engineering, logistics, management and technical services including information technology services are provided by VSE and by each of its subsidiaries and divisions. Subsidiaries include Energetics Incorporated ("Energetics"), Human Resource Systems, Inc. ("HRSI"), Ship Remediation and Recycling, Inc. ("SRR") (formerly VSE Services Corporation ("VSES")), and VSE Services International Inc. ("VSI") incorporated in August 1999. Divisions include BAV Division ("BAV"), Fleet Maintenance Division ("Fleet Maintenance") formed in June 1999, VSE IT Services Division ("IT Services") formed in January 1999, Indian Head Division ("Ordnance"), and Value Systems Services Division ("VSS").

Software products and services include sales of developed software products and

the services related to the installation and use of the software. This is the primary business of VSE's former subsidiary CMstat Corporation ("CMstat"), sold in May 1999. (See "Divestiture" below).

<TABLE>

The following table sets forth certain items including consolidated revenues, pretax income and net income, and the changes in these items by segment for the three and nine month periods ended September 30, 1999 and 1998 (in thousands). The revenues, pretax losses and net losses of the SPS segment for the three and nine month periods ended September 30, 1999 include the activity of CMstat through May 21, 1999.

<CAPTION>

	1999		Compared		to	
	Three Months	Nine Months	1998	Three	Nine	
	Ended September 30,	Ended September 30,	Three	Months	Months	
	1999	1998	1999	1998	Months	Months
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Engineering, Logistics, Management and Technical Services Segment:						
Revenues	\$36,609	\$44,203	\$122,848	\$123,419	\$(7,594)	\$ (571)
Pretax income	\$ 1,124	\$ 1,197	\$ 2,844	\$ 3,316	\$ (73)	\$ (472)
Provision for income taxes	449	350	1,132	1,224	99	(92)
Net income	\$ 675	\$ 847	\$ 1,712	\$ 2,092	\$ (172)	\$ (380)

VSE CORPORATION AND SUBSIDIARIES
Management Discussion and Analysis

	1999		Compared		to	
	Three Months	Nine Months	1998	Three	Nine	
	Ended September 30,	Ended September 30,	Three	Months	Months	
	1999	1998	1999	1998	Months	Months
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Software Products and Services Segment:						
Revenues	\$ 0	\$ 880	\$ 902	\$ 2,358	\$(880)	\$(1,456)
Pretax loss	\$ 0	\$(285)	\$(1,478)	\$(1,712)	\$ 285	\$ 234
Benefit for income taxes	0	(111)	(670)	(660)	111	(10)
Net loss	\$ 0	\$(174)	\$(808)	\$(1,052)	\$ 174	\$ 244

</TABLE>

RESULTS OF OPERATIONS

The discussion and analysis which follows is intended to assist in understanding and evaluating the results of operations, financial condition, and certain other matters of the company. The company is engaged principally in providing engineering, testing, and management services to the U.S. Government (the "government") and software products and related services to commercial customers. All significant intercompany transactions have been eliminated in consolidation. Certain prior year balances have been reclassified for comparative purposes.

Engineering, Logistics, Management and Technical Services Segment

Revenues for this segment declined by less than 1% for the nine month period ending September 30, 1999, as compared to the same period of 1998. A decrease in the level of services ordered by HRSI's customers during the first nine months of 1999 was substantially offset by increased revenues in the company's other business units. Revenues for the three month period ending September 30, 1999, decreased by approximately 17% as compared to the same period of 1998. The decrease in revenues for this three month period is primarily due to the timing of BAV revenue from quarter to quarter. (See "BAV Contract" below).

Pretax income for this segment decreased by approximately 6% for the three month period and by approximately 14% for the nine month period ending September 30, 1999, as compared to the same periods of 1998. The decrease for the nine month period was due primarily to the decrease in work performed by VSE in 1999 without a corresponding timely decrease in indirect costs. In addition to the sale of the SPS segment (See "Divestiture" below), the company is continuing the process of restructuring which includes continued emphasis and focus on decreasing its indirect costs. The decrease in pretax income for the three month period was due primarily to the decrease in profits associated with the decline in HRSI revenues in 1999 as compared to 1998.

VSE CORPORATION AND SUBSIDIARIES Management Discussion and Analysis

The largest customer for the engineering, logistics, management and technical services rendered by the company is the U.S. Department of Defense ("Defense"), including agencies of the U.S. Army, Navy, and Air Force. VSE's engineering services revenues have historically been subject to annual fluctuations resulting from changes in the level of Defense spending. Accordingly, there can be no assurance that future reductions in Defense spending will not have a material adverse impact on the company's results of operations or financial position.

Substantially all of the company's revenues from this segment depend on the award of new contracts, on current contracts not being terminated for the convenience of the government, on the exercise of option periods, and the satisfaction of incremental funding requirements on current contracts. In 1999 and 1998, the company did not experience any termination of contracts for the convenience of the government or any non-exercise of option periods on current contracts which were material to the company's ongoing results of operations or financial position.

BAV Contract. In August 1995, VSE's BAV Division was awarded a contract with the U.S. Navy to provide engineering, technical and logistical support services associated with the sale, lease, or transfer of Navy ships to foreign governments. BAV began work on the contract in September 1995. This contract has the potential, if all options are exercised, to generate revenues in excess of one billion dollars over a ten year period from 1995 through 2005.

The contract accounted for approximately 52% and 50% of consolidated revenues from operations during the nine month periods ending September 30, 1999 and 1998, respectively. The level of revenues generated by this contract will vary depending on a number of factors including the timing of ship transfers and associated support services ordered by foreign governments and economic conditions of potential customers worldwide. The company has experienced significant quarterly revenue fluctuations and anticipates that future quarterly revenues will be subject to significant variations primarily due to changes in the level of activity on this contract.

New Business. The company has been successful in bidding and winning new types of work in the ELMTS segment. VSE IT Services was formed in January 1999 to bid and perform on work issued through the government's GSA schedule. This division was awarded a second purchase agreement in October 1999 to support the U.S. Navy's Engineering Investigations (EI) safety program related to naval aircraft and aircraft systems and subsystems, and is expected to begin work in November 1999.

VSI was formed in August 1999 to expand VSE's international presence and perform services for foreign governments and commercial customers similar to the services it has traditionally provided in the United States. VSI received its

first work order in September 1999.

VSE CORPORATION AND SUBSIDIARIES

Management Discussion and Analysis

SRR is a part of a joint venture that was awarded a contract associated with a new government program to dismantle and recycle retired U. S. Navy ships. The contract award was protested and SRR has not begun work on the contract pending resolution of the protest.

Software Products and Services Segment

The company sold its CMstat subsidiary in May 1999. (See "Divestiture" below). The revenues and pretax losses of this segment for the nine month periods ending September 30, 1999, include the activity of CMstat through May 21, 1999, and the pretax loss includes a loss on sale. Accordingly, year to year comparisons of revenue and income for this segment are not meaningful. As a result of the sale of CMstat, the company will no longer have any active business operations in the software products and services segment.

Divestiture

On May 21, 1999, VSE sold its wholly owned subsidiary CMstat Corporation which comprised 100% of the business activity of the SPS segment. Under terms of the sale, VSE transferred 100% of the outstanding capital stock of CMstat to a company wholly-owned by CMstat's CEO in exchange for fixed assets valued at approximately \$342 thousand and an \$800 thousand promissory note for which principal and interest is payable in installments between September 1, 1999 and May 20, 2006. The transaction resulted in a net loss of approximately \$574 thousand to VSE.

Liquidity and Capital Resources

Cash and cash equivalents increased by approximately \$239 thousand during the nine month period ended September 30, 1999. Cash from operating activities of approximately \$2 million was used to finance investing activities of approximately \$1.2 million and to reduce financing requirements by approximately \$600 thousand. Significant investing activities included purchases of property and equipment of approximately \$977 thousand. Significant financing activities included reduced borrowing on the company's bank loan, including commitments for checks outstanding, of approximately \$365 thousand and the payment of cash dividends of approximately \$229 thousand.

A net increase in cash and cash equivalents of approximately \$300 thousand during the nine month period ending September 30, 1998, resulted from approximately \$3.9 million provided by operating activities, approximately \$3.2 million used in financing activities, and approximately \$400 thousand used in investing activities. Significant financing activities included reduced borrowing on the company's bank loan, including commitments for checks outstanding, of approximately \$3.1 million. Significant investing activities included purchases of property and equipment of approximately \$524 thousand.

VSE CORPORATION AND SUBSIDIARIES

Management Discussion and Analysis

The difference between the cash provided by operating activities of approximately \$2 million in 1999 as compared to approximately \$3.9 million in 1998 is primarily due to the reduction in assets and liabilities associated with the sale of CMstat. The effect of the CMstat sale on cash provided by operating activities was offset somewhat by changes in the levels of accounts receivable and accounts payable associated with fluctuations in BAV contract activity.

The company's principal requirements for cash are to finance the costs of operations pending the collection of accounts receivable, to acquire capital assets for office and computer support, to pay cash dividends, and to finance internal research and development. Performance of work under the BAV contract

has the potential to cause substantial requirements for cash; however, management believes that the cash flows from future operations and the bank loan commitment are adequate to meet current operating cash requirements.

VSE's requirements for working capital are affected significantly by its revenues and accounts receivable, which are primarily from billings made by the company to the government or other government prime contractors for services rendered. Such accounts receivable generally do not present liquidity or collection problems. Working capital is also affected by (a) contract retainages, (b) start-up and termination costs associated with new or completed contracts, (c) capital equipment requirements, (d) differences between the provisional billing rates authorized by the government compared to the costs actually incurred by the company, and (e) profitability.

Government contracts generally require VSE to pay for material and subcontract costs included in VSE's contract billings prior to receiving payment for such costs from the government. However, such contracts generally provide for progress payments on a monthly or semimonthly basis, thereby reducing requirements for working capital.

Quarterly cash dividends at the rate of \$.036 per share were declared during the three month period ending September 30, 1999. Pursuant to its bank loan agreement, the payment of cash dividends by VSE is subject to a maximum annual rate. VSE has paid cash dividends each year since 1973.

ESOP Advances

During 1998, 1997 and 1996, the company advanced the ESOP trust \$112 thousand, \$330 thousand and \$350 thousand, respectively, in connection with distributions made to terminated participants. In December 1998, the company purchased 72,000 shares of VSE stock from the ESOP at market price and the ESOP simultaneously returned the proceeds of \$792 thousand from the stock sale to the company as repayment of the advances.

VSE CORPORATION AND SUBSIDIARIES

Management Discussion and Analysis

Inflation and Pricing Policy

Most of the contracts performed by VSE provide for estimates of future labor costs to be escalated for any option periods provided by the contracts, while the non-labor costs included in such contracts are normally considered reimbursable at cost. VSE property and equipment consists principally of computer systems equipment and furniture and fixtures. The overall impact of inflation on replacement costs of such property and equipment is expected to be insignificant.

Global Economic Conditions

VSE's business is subject to the risks arising from global economic conditions associated with potential foreign customers served through VSE's contracts with the U.S. Government. Adverse economic conditions in certain parts of the world could potentially affect BAV sales. Management is unable to predict what, if any, impact such conditions may have on the company's financial position or results of operations.

Year 2000

Overview. The "Year 2000" issue, or the inability of many computerized systems to properly recognize a date in the year 2000, could potentially affect the company's ability to perform many common business functions. The company recognizes the impact that this could have on its operating and financial results and has implemented a Year 2000 Action Plan ("Y2K Plan") to address the issue. The Y2K Plan includes: 1) Assignment of compliance responsibilities to operating managers, staff directors, information technology staff, contract administration and procurement staff, and the Comptroller. Additionally, the company has assigned a Senior Vice President to serve as the Y2K Coordinator, with responsibility for ensuring development and implementation of the Y2K Plan;

- 2) Development of a Y2K Communications System to ensure proper information dissemination and reporting with regard to Year 2000 compliance efforts; and
- 3) Development and implementation of a Year 2000 Compliance Program ("Y2K Program").

State of Readiness. Ongoing assessments of the impact of the Year 2000 issue on systems and operations have been formalized into the Y2K Program. The Y2K Program includes phases for awareness, inventory and assessment, correction and renovation (including validation and testing and implementation), and contingency planning.

Awareness. Managers have been informed about the nature of the Year 2000 problem and what efforts the company is undertaking to address it. This includes: distribution of reference materials and lists of vendor certified Year 2000 compliant hardware, equipment, and software; selection of contact points for each location and organization for Year 2000 compliance issues; and assignment of responsibility for ensuring that operations are not disrupted or are only minimally affected. At this time, all of the company's initially

VSE CORPORATION AND SUBSIDIARIES

Management Discussion and Analysis

identified efforts associated with the awareness phase have been completed. Additional awareness efforts, if any, will be made as they become known.

Inventory and Assessment. Identification has been made of all "Mission Critical" actions or functions and of all hardware, equipment, software, and embedded systems used to conduct the "Mission Critical" actions or functions. "Mission Critical" is defined as an action or function that must happen in order to serve a customer or line of business comprising more than 10% of the revenue base or pre-tax profit of an organization within the company. This phase includes: 1) Developing inventory listings of all hardware, equipment, software, embedded systems, operating systems, custom user applications, and contract obligations having a Year 2000 impact; 2) Analyzing and developing corrective actions for each of the items on the inventory listings; 3) Procuring programs and tools to provide compliance for the items on the inventory listings; and 4) Surveying manufacturers and vendors to obtain certification of their products as Year 2000 compliant. The inventory and assessment phase is approximately 100% complete. Analysis of the items on the inventory listing has been done primarily using internally administered programs supplied by independent outside sources. Approximately 99% of the hardware, equipment, and embedded systems and approximately 90% of the software, operating systems, custom user applications and contract obligations on the inventory listing have been found to be Year 2000 compliant or have been removed from service.

Correction and Renovation. The items identified in the inventory and assessment phase have been redesigned, repaired, converted, or replaced, as necessary, to ensure Year 2000 compliance. Corrections and renovations are documented and this documentation is distributed to the affected managers and staff. Testing plans are developed and validation and testing occurs. Risk analysis is conducted and contingency planning issues are identified. The correction and renovation phase is approximately 88% completed and is expected to be completed prior to the end of November of 1999.

Costs. Costs incurred to date for Year 2000 compliance efforts have been minimal and are included as part of the company's ongoing administrative costs and have not been separately identified. The company continues to upgrade and improve its information technology systems as part of its normal effort to maintain a competitive edge. As these upgrades and improvements are made, the company is ensuring that all are Year 2000 compliant. Therefore, the majority of costs incurred for computer systems that ensure Year 2000 compliance are expenditures that are made in the normal course of business. Total property and equipment expenditures for 1998, including expenditures for computers and computer systems, were approximately \$1.6 million. Expenditures for 1999 are expected to remain at about the same level. Accordingly, management believes that the incremental costs of ensuring that the company's information technology systems are Year 2000 compliant will not materially affect the company's consolidated financial position, liquidity, or results of operations through December 31, 1999.

Risks. The full range of potential risks associated with the Year 2000 issue is

under review. Potential risks include obligations related to contract performance on current and past contracts, the reliance on infrastructure

VSE CORPORATION AND SUBSIDIARIES

Management Discussion and Analysis

services to conduct the company's business operations, and the possibility of liquidity issues caused by payment problems with VSE's banks or government customers. Although management believes that the risks associated with internal issues regarding the Year 2000 problem will be minimal, the risks associated with external issues are difficult to predict. If these external issues cause massive failures to systems upon which the company is reliant, the results could materially affect the company's consolidated financial position, liquidity, or results of operations.

The government agency that pays the majority of the company's billings, the Defense Finance and Accounting Service ("DFAS"), has issued published assurances that it is diligently pursuing a Year 2000 compliance strategy and is confident that its payments to contractors will continue uninterrupted in January 2000. The company's primary bank has also issued published statements that it is year 2000 compliant and that banking transaction activity will not be interrupted.

Contingency Plans. The Y2K Plan calls for the development of contingency plans. VSE currently has extra borrowing capacity under its bank loan agreement and intends to maintain this extra borrowing capacity beyond the year 2000 to provide funding in the event of government customer payment problems. Contingency plans related to contract performance obligations and to business operation infrastructure services have been developed in a preliminary form and are scheduled to be finalized and in place by the first of December 1999. The company will perform some testing on certain aspects of the contingency plans during December 1999.

Market Risk

The company does not use derivative instruments to alter the interest characteristics of its debt instruments. The aggregate fair value of the company's financial instruments approximates the carrying value at September 30, 1999.

Forward Looking Statements

This filing contains statements which, to the extent they are not recitations of historical fact, constitute "forward looking statements" under federal securities laws. All such statements are intended to be subject to the safe harbor protection provided by applicable securities laws. For discussions identifying some important factors that could cause actual VSE results to differ materially from those anticipated in the forward looking statements contained in this statement, see VSE's Securities and Exchange Commission filings including, but not limited to, VSE's Annual Report on Form 10-K for the fiscal year ended December 31, 1998 (Form 10-K), including discussions contained in VSE's "Letter to Stockholders"; "VSE Operations"; "Description of Business"; "Management Discussion and Analysis"; and "Notes to Consolidated Financial Statements" in the VSE Corporation 1998 Annual Report incorporated by reference and attached to VSE's Form 10-K filing.

VSE CORPORATION AND SUBSIDIARIES

PART II. Other Information

Item 6. Exhibits and Reports on Form 8-K.

(a) Exhibits.

None.

(b) Reports on Form 8-K.

None.

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has omitted all other items contained in "Part II. Other Information" because such other items are not applicable or are not required if the answer is negative or because the information required to be reported therein has been previously reported.

VSE CORPORATION AND SUBSIDIARIES

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.

VSE CORPORATION

/s/ C. S. WEBER

Date: October 29, 1999

C. S. Weber, Senior Vice President,
and Secretary

/s/ T. J. CORRIDON

Date: October 29, 1999

T. J. Corridon, Senior Vice President
and Chief Financial Officer
(Principal Financial Officer)

/s/ T. R. Loftus

Date: October 29, 1999

T. R. Loftus, Vice President and
Comptroller
(Principal Accounting Officer)

The financial information included in this report reflects all known adjustments normally determined or settled at year-end which are, in the opinion of management, necessary to a fair statement of the results for the interim periods. The accompanying notes to consolidated financial statements are an integral part of this report.

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