SELECTED INVESTOR QUESTIONS RECEIVED THROUGH APRIL 19, 2018

Question
There has been a lot of capital deployed during Q1 so far (based on YTD information released in Q4 filings), more than in many whole years in the recent past.

While I understand it's not possible to know with certainty, what is your best estimate on the ratio of that capital that has been deployed by recent additions to the M&A effort, and what came from the same core M&A team that has been there for a long time?

In other words, how much is it the luck of the draw (sometimes a whole bunch of big things close at the same time randomly), and how much is a result of scaling up the M&A team, and possibly more sustainable when it comes to acquisition run-rate going forward, as far as you can determine?

Response
Excluding the Acceo acquisition, the increased acquisition activity is primarily the result of us scaling up the M&A team.

Question
To what extent are you involved in providing Cyber Security solutions for your customer base? What kind of business do you expect from the Federal Government and their emphasis on dealing with Cyber Security threats?

Response
Cyber security solutions do no generate any significant revenue for Constellation.

Question
What effort has been put in place to retain employees from creating copy cat firms with a similar mandate? On a larger scale, how do you plan on competing with larger private equity firms that also specialize in technology investments that can pay more?

Response
We offer our employees the opportunity to invest, compound capital, and over time build a large portfolio of software companies within Constellation. Those that do this well can generate significant wealth.

With regards to competing against private equity: hopefully the benefits of CSI ownership (a permanent home for the business where the management team will have autonomy and access to literally hundreds of peer companies with similar issues and opportunities) will outweigh any benefits of selling to private equity.

Question
About not decreasing adjusted earnings to reflect the minority interest in earnings. I realise that accounting rules reflect the minority interest in TSS in a liability rather than in minority earnings. However, management adds back the full change in that liability for adjusted earnings. It seems to me that this means that the minority interest in TSS earnings while recognised as a liability in GAAP becomes totally unrecognised in adjusted earnings. Why is that appropriate? I realise that the minority interest would be a non-cash expense. But should it not still be recognised in adjusted earnings? Or, by adjusted earnings does management mean to arrive at a cash flow number? I have been an owner of Constellation off and (mostly) on for over seven years and have read its reports and letters closely all these years. I greatly respect the success and openess of the company.

Response

Adjusted net income is a metric that is intended to be a proxy for the cash generated in a period that's available to Constellation's shareholders. Our calculation of Adjusted net income excludes the 33.29% non-controlling interest in the Adjusted net income of TSS.

Question

About adjusted earnings. In my (long) experience, when items are added back to adjust earnings, it is almost always done on a tax-affected basis to reflect that the added back expense reduced GAAP if not cash taxes. Constellation does not appear to tax -affect the adjustments. That seems less conservative to me. Please explain. My guess is that it is because Constellation is trying to calculate some measure of cash and not adjusted earnings? I have been an owner of Constellation off and (mostly) on for over seven years and have read its reports and letters closely all these years. I greatly respect the success and openess of the company. I have had the greatest respect for Mark Leonard for many years but I am growing concerned that the adjusted earnings figure seems aggressive. Am I wrong?

Response

Adjusted net income is a metric that is intended to be a proxy for the cash generated in a period that's available to shareholders. The largest add-back in the ANI number is the amortization of intangibles associated with acquisitions. Our contention, is that this is non-economic amortization, and that the intangible value of our underlying assets is actually increasing and hence the full amount of the amortization should be added to ANI.

Question

Tyler technologies says the public sector software market is growing at 6%-7% per annum and their own organic growth has been in the 10%-12% range. Why are your public sector businesses growing at substantially below market growth rates at 2%-3%?

Response

One of the main contributors to the lower growth is our exposure to the US healthcare market which rolls up into our "Public Sector" reporting segment.

Question

You regularly talk about how decentralized CSI is and how you prefer to break up bigger teams into smaller teams rather than attempt economies of scale by aggregating teams together.

Would this apply to the operating groups and how would you think about this? Would you ever break up an operating group into two because it too large, or are things decentralized enough within the groups to allow them to become quite a bit larger than they are now? How did the company arrive at the current number of operating groups and why is that the right number at this time? Is the bottleneck for more groups down the line the number of executives capable of running a group, or something else?

Response

We break up business units to enhance their customer focus. The operating groups are now essentially mini Constellations. The same way Constellation's head office pushed down responsibility as we grew, the operating groups are pushing down responsibility to the layer beneath them (the group we refer to as portfolio managers). Over time the portfolio managers will become mini Constellations and the cycle will repeat.

The number of operating groups under Constellation will be limited to the number of direct reports that Mark Leonard is comfortable managing.

An important item to keep in mind, is that we are not doctrinaire about organizational structure: we are willing to cater to exceptional people with exceptional talents who wish to ply their trade using unique reporting relationships or capital deployment models.