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DEANNA H. LUND, ANDREW M. LEITCH, LAURA  
13 SIEGAL, NAOMI D. WHITACRE, GEORGE  
WOZENCRAFT, and WILLIAM MAZILLY; and Specially  
14 Appearing Defendants FARZAD GHASSEMI, GREGORY  
JACOBSEN, SCOTT I. ANDERSON, SCOT JARVIS, and  
15 WILLIAM HOGLUND

16  
17 UNITED STATES DISTRICT COURT  
18 SOUTHERN DISTRICT OF CALIFORNIA

19  
20 IN RE WIRELESS FACILITIES, INC.,  
DERIVATIVE LITIGATION

Case No. 04-CV-1663 JAH (NLS)

**STIPULATION AND  
AGREEMENT OF SETTLEMENT  
OF DERIVATIVE CLAIMS**

21  
22 \_\_\_\_\_  
This Document Relates to:

23 ALL ACTIONS.

24 This Stipulation and Agreement of Settlement of Derivative Claims (“Stipulation”), to be  
25 effective as of January 5, 2010, is made and entered into pursuant to Rule 23.1 of the Federal  
26 Rules of Civil Procedure. This Stipulation contains the terms of a settlement (the “Settlement”)  
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1 among Settling Defendants and Plaintiffs<sup>1</sup>, for themselves and derivatively on behalf of Kratos  
2 Defense & Security Solutions, Inc. (formerly known as Wireless Facilities, Inc.) (“Kratos” or the  
3 “Company”), in connection with *In re Wireless Facilities, Inc. Derivative Litigation*, Master File  
4 No. 04-CV-1663 JAH (NLS) (the “Federal Action”), currently pending in this Court, and *In re*  
5 *Wireless Facilities, Inc. Derivative Litigation*, GIC 834253 (the “State Action”), currently  
6 pending in the Superior Court of the State of California, County of San Diego (collectively, the  
7 “Derivative Actions”).

8 The Stipulation is intended by the Settling Parties to fully, finally, and forever resolve,  
9 discharge, and settle the Released Claims and the Derivative Actions upon and subject to the  
10 terms and conditions hereof and subject to the approval of the Court.

#### 11 **I. THE DERIVATIVE ACTIONS**

12 On August 4, 2004, Kratos announced, following an extensive analysis of its contingent  
13 tax liabilities, its intention to restate its financial statements for fiscal years ended 2000  
14 through 2003 to accrue for certain foreign tax contingencies. Kratos preliminarily estimated an  
15 aggregate increase of expenses between \$10 and \$12 million for those three years. Kratos also  
16 announced that it would consider other adjustments related to issues identified as immaterial in  
17 prior years.<sup>2</sup>

18 The day after the Company’s August 4 announcement, and roughly a month before it  
19 released further details of the restatement, the first of fourteen lawsuits — ten federal securities  
20 class actions, two federal derivative actions, and two state derivative actions — was filed. The  
21 ten securities class actions were subsequently consolidated into a single action before this Court  
22 — *In re Wireless Facilities, Inc. Securities Litigation*, Master File No. 04-CV-1589 JAH (NLS)

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24 <sup>1</sup> Unless otherwise defined herein, capitalized words or terms have the meaning as set  
25 forth below in the “Definitions” section.

26 <sup>2</sup> On September 20, 2004, Kratos filed its FY:03 Form 10-K/A, which detailed the  
27 announced restatement. In the restatement, Kratos made an approximately \$11 million  
28 adjustment for tax contingencies, in line with its August 4, 2004 estimate, as well as additional  
adjustments totaling approximately \$30 million over the three-year period.

1 (S.D. Cal) (the “2004 Federal Class Action”).<sup>3</sup> Similarly, in 2005 the two federal derivative  
2 lawsuits, brought separately by Federal Plaintiffs Michael Roth and Rosario Pedicini, were  
3 consolidated into the Federal Action. The two state derivative lawsuits, brought separately by  
4 State Plaintiffs Mary Beth Joseph and Robert Casden, were consolidated into the State Action.<sup>4</sup>

5 In March 2005, Federal Plaintiffs filed their Consolidated Verified Shareholder Derivative  
6 Complaint (“Consolidated Complaint”) against sixteen current or former officers, directors, and  
7 employees of Kratos.<sup>5</sup> Federal Plaintiffs alleged that these individuals failed to properly account  
8 for foreign tax contingencies, failed to exercise appropriate oversight, engaged in unlawful insider  
9 trading, and breached their fiduciary duties to the Company. Federal Plaintiffs asserted eight  
10 causes of action in their original Consolidated Complaint, which were related to the Company’s  
11 announcement that it would restate its financial statements for fiscal years 2000 to 2003. The  
12 claims were also related to Federal Plaintiffs’ allegation that the defendants knew about material  
13 misstatements in the Company’s accounting.

14 In May 2005, six of the individual defendants named in the Consolidated Complaint —  
15 Messrs. Gregory (“Jacobsen”), Farzad Ghassemi (“Ghassemi”), William Hoglund (“Hoglund”),  
16 Scott I. Anderson (“Anderson”), Scot Jarvis (“Jarvis”), and William Owens (“Owens”) — filed a  
17 motion to dismiss for lack of personal jurisdiction. The other individual defendants moved to  
18 dismiss the Consolidated Complaint for failure to allege adequately the elements of the causes of  
19 action. Additionally, Kratos moved to dismiss based on Federal Plaintiffs’ purported failure to  
20 either make a pre-suit demand or plead with particularity why demand was excused. The  
21 Company also moved for a temporary stay pending resolution of the 2004 Federal Class Action.  
22 At the request of this Court, in March 2006, all of the defendants withdrew their respective

23 <sup>3</sup> On September 3, 2008, this Court preliminarily approved settlement of the 2004 Federal  
24 Class Action. On January 13, 2009, following a motion by the parties, this Court granted final  
25 approval of the proposed settlement terms, issued its final judgment on the matter, and entered an  
order dismissing the case with prejudice.

26 <sup>4</sup> Prior to any response by the defendants to the State Action, the matter was stayed (and  
remains so) by the San Diego Superior Court pending resolution of the Federal Action.

27 <sup>5</sup> In addition, Kratos was named as a nominal defendant.  
28

1 motions without prejudice so that the Court could first determine its jurisdiction over the  
2 Specially Appearing Defendants.

3 Federal Plaintiffs deposed and propounded interrogatories upon those defendants who  
4 moved to dismiss for lack of personal jurisdiction. On March 20, 2007, the Court granted the  
5 motion as to Messrs. Jacobsen, Ghassemi, Hoglund, Anderson, and Jarvis, dismissing them from  
6 the case. However, the Court determined that it had jurisdiction over Mr. Owens.

7 On March 12, 2007, Kratos announced that it was conducting an internal investigation  
8 into its historical stock option grant practices going back to 1998. Kratos also announced that it  
9 had identified some option “grants issued between 1998 and 2003 that require[d] further review  
10 because their historical measurement dates appear[ed] incorrect and [were] expected to result in  
11 adjustments affecting previously issued financial statements.” The announcement stated that it  
12 was likely that Kratos would restate its financial statements for fiscal years 2000 to 2005.

13 On March 27, 2007, two weeks after the Company’s public announcement that it was  
14 conducting the internal stock option review, Federal Plaintiffs filed their Verified Consolidated  
15 Amended Shareholder Derivative Complaint for violations of California Corporations Code,  
16 Breach of Fiduciary Duty, Abuse of Control, Gross Mismanagement, Waste of Corporate Assets,  
17 Unjust Enrichment, Violations of the Sarbanes-Oxley Act of 2002, Accounting, Recission and  
18 Constructive Trust (“Amended Complaint”) against all of the individuals originally named in the  
19 prior Consolidated Complaint, including those previously dismissed for lack of jurisdiction.  
20 Federal Plaintiffs also added nine new defendants, including William Mazilly (“Mazilly”), who  
21 asserted that he was a resident of Louisiana.

22 The Amended Complaint contains the original financial reporting and accounting  
23 allegations regarding the 2004 restatement and added new allegations that certain defendants  
24 “backdated” or “springloaded” employee stock option grants so that the options were granted at  
25 less than fair market value. Federal Plaintiffs asserted five new causes of action in the Amended  
26  
27  
28

1 Complaint, each relating to the Company's announcement that it was conducting an internal  
2 investigation into its stock option grant practices.<sup>6</sup>

3 On July 2, 2007, the five defendants previously dismissed for lack of personal jurisdiction,  
4 joined now by Mr. Mazilly, moved to dismiss the Amended Complaint on the ground that the  
5 Court still lacked jurisdiction over them despite the new stock option allegations. Again, the  
6 remaining defendants were not required to respond to the Amended Complaint until the Court  
7 determined the jurisdictional issues. Federal Plaintiffs opposed the motion to dismiss on  
8 September 25, 2007.

9 On February 26, 2008, the Court granted the jurisdictional motion to dismiss as to the  
10 previously-dismissed defendants. However, the Court determined that it had jurisdiction over Mr.  
11 Mazilly. Federal Plaintiffs subsequently moved the Court, pursuant to Federal Rule of Civil  
12 Procedure 54(b), for certification and entry of final judgment of the Court's February 2008 Order  
13 so that Federal Plaintiffs might appeal the Order to the Ninth Circuit Court of Appeals. The  
14 defendants to the Federal Action took no position with respect to Federal Plaintiffs' Rule 54(b)  
15 motion, but instead requested that in the event the Court granted the motion and certified the  
16 jurisdictional Order, that the Court stay all proceedings in the matter unrelated to personal  
17 jurisdiction pending the appeal.

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19 <sup>6</sup> In April 2007, purported Kratos stockholder Eamen Hameed filed a federal derivative  
20 complaint purportedly on behalf of Kratos and against a subset of the same current and/or former  
21 officers and directors named in the Federal and State Actions — *Hameed v. Tayebi*, No. 07-CV-  
22 0680 BTM (RBB) (S.D. Cal.) (the "Hameed Action"). The Hameed Action arose from Kratos'  
23 March 2007 announcement that it was conducting the internal stock option review and alleged  
24 that certain defendants allowed company insiders to backdate stock option grants, so that stock  
25 options were priced below fair market value on the day they were actually granted, and that as a  
26 result, Kratos' relevant U.S. Securities and Exchange Commission ("SEC") filings were false  
27 and misleading. On August 18, 2008, Hameed voluntarily dismissed the Hameed Action  
28 pursuant to Federal Rule of Civil Procedure 41(a). Additionally, in November 2007, a  
consolidated federal class action securities lawsuit — *In re Wireless Facilities, Inc. Securities  
Litigation II*, Master File No. 07-CV-00482-BTM (NLS) (S.D. Cal.) (the "2007 Federal Class  
Action") — was filed in this Court, alleging that Kratos backdated or springloaded employee  
stock option grants. On September 3, 2008, this Court preliminarily approved settlement of the  
2007 Federal Class Action. On December 19, 2008, this Court granted final approval of the  
proposed settlement terms, issued its final judgment on the matter, and entered an order  
dismissing the case with prejudice.

1 On July 10, 2008, the Court granted Federal Plaintiffs' motion for certification, but held  
2 that a stay of all unrelated proceedings was premature at that time. On August 12, 2008, Federal  
3 Plaintiffs filed a notice of appeal of the jurisdictional order.

4 On August 25, 2008, in an effort to resolve the Derivative Actions, the Settling Parties  
5 mediated the matters before Judge Daniel Weinstein (Ret.) of JAMS. While a settlement  
6 agreement was not reached during the mediation, the Settling Parties, along with the assistance of  
7 the mediator, continued to pursue extensive good-faith settlement negotiations. In addition,  
8 certain of the Settling Parties participated in further in-person meetings with the mediator in  
9 February 2009. While a settlement agreement was not reached following the February 2009  
10 meetings, the Settling Parties, along with the assistance of the mediator, continued to pursue  
11 additional extensive good-faith settlement negotiations. In October 2009, the Settling Parties  
12 agreed in principle to settle the Derivative Actions on terms set forth in this Stipulation and  
13 subject to Court approval.

## 14 **II. PLAINTIFFS' CLAIMS AND BENEFITS OF SETTLEMENT**

15 Plaintiffs believe that the claims asserted in the Derivative Actions have merit. However,  
16 Plaintiffs' Counsel recognize and acknowledge the expense and length of continued proceedings  
17 necessary to prosecute the Derivative Actions on behalf of Kratos through at least one appeal and  
18 potentially through trial. Plaintiffs' Counsel have conducted an investigation of the claims  
19 asserted in the Derivative Actions, including research of publicly available information and  
20 review of certain documents requested by and provided to Plaintiffs' Counsel by Kratos and  
21 certain defendants. Plaintiffs' Counsel also have taken into account the uncertain outcome and  
22 the risk of any litigation, especially in complex actions such as the Derivative Actions, as well as  
23 the difficulties and delays inherent in such litigation. Plaintiffs' Counsel also are mindful of the  
24 inherent problems of proof of, and possible defenses to, the causes of action asserted in the  
25 Derivative Actions. Plaintiffs' Counsel believe that the Settlement set forth in this Stipulation  
26 confers substantial benefits upon, and is in the best interest of, Kratos, its shareholders, and  
27 Plaintiffs.

28

1     **III.     SETTLING DEFENDANTS' DENIAL OF WRONGDOING AND LIABILITY**

2             The Settling Defendants have denied and continue to deny each and all of the claims and  
3 contentions alleged in the Derivative Actions. The Individual Defendants expressly have denied  
4 and continue to deny all charges of wrongdoing or liability against them or any of them arising  
5 out of any of the conduct, statements, acts, or omissions alleged, or that could have been alleged,  
6 in the Derivative Actions. The Individual Defendants also have denied and continue to deny,  
7 *inter alia*: (i) that they violated the federal securities laws, violated state law, or breached their  
8 fiduciary duties; (ii) the allegations that Kratos has suffered damage; (iii) that the price of Kratos  
9 securities was artificially inflated by reason of alleged misrepresentations, non-disclosures, or  
10 otherwise; (iv) that Kratos was harmed by any of the conduct alleged in the Derivative Actions;  
11 and (v) that a majority of the Board of Kratos was not independent and disinterested during the  
12 relevant periods.

13             Nonetheless, the Settling Defendants have concluded that further conduct of the  
14 Derivative Actions would be protracted, expensive, and distracting to themselves, Kratos, and its  
15 management, and that it is desirable and beneficial to them that the Derivative Actions be fully  
16 and finally settled in the manner and upon the terms and conditions set forth in this Stipulation, in  
17 order to limit further expense, inconvenience, and distraction, and to dispose of the burden of  
18 protracted litigation. The Settling Defendants have also taken into account the uncertainty and  
19 risks inherent in any litigation, especially in complex cases like these Derivative Actions. Kratos  
20 has determined that it is in its best interest to enter into this Stipulation because Kratos will  
21 receive substantial benefits from the agreed-upon Settlement.

22     **IV.     TERMS OF STIPULATION AND AGREEMENT OF SETTLEMENT**

23             NOW, THEREFORE, IT IS HEREBY STIPULATED AND AGREED by and among  
24 Plaintiffs (on behalf of themselves and derivatively on behalf of Kratos), nominal defendant  
25 Kratos, and the Individual Defendants, by and through their respective counsel or attorneys of  
26 record, that, subject to the approval of the Court, the Derivative Actions and the Released Claims  
27 shall be finally and fully compromised, settled, and released, and the Derivative Actions shall be  
28

1 dismissed with prejudice as to the Settling Parties, upon and subject to the terms and conditions of  
2 the Stipulation, as follows:

3 **1. Definitions**

4 As used in this Stipulation, the following terms have the meanings specified below:

5 1.1 “Court” means the United States District Court for the Southern District of  
6 California.

7 1.2 “Current Kratos Stockholders” — for purposes of publication of the Summary  
8 Notice of Pendency and Settlement of Derivative Actions and the Notice of Pendency and  
9 Settlement of Derivative Actions — means all record and beneficial owners of Kratos capital  
10 stock of all classes and series on the date the Stipulation is executed.

11 1.3 “D&O Insurers” means Kratos’ applicable director and officer liability coverage  
12 insurance providers.

13 1.4 “Effective Date” means the first date by which all of the events and conditions  
14 specified in ¶8.1 of this Stipulation have been met and have occurred.

15 1.5 “Federal Plaintiffs” means Rosario Pedicini and Michael Roth.

16 1.6 “Fees and Expenses Payment” means the payment of Plaintiffs’ Counsels’  
17 attorneys’ fees and expenses as contemplated by ¶¶5.1-5.3 of the Stipulation.

18 1.7 “Final” means the latest of: (a) the date of final affirmance on an appeal of the  
19 Judgment, the expiration of the time for a petition for or a denial of a writ of certiorari to review  
20 the Judgment and, if certiorari is granted, the date of final affirmance of the Judgment following  
21 review pursuant to that grant; (b) the date of final dismissal of any appeal from the Judgment or  
22 the final dismissal, denial or withdrawal of any proceeding on certiorari to review the Judgment;  
23 or (c) if no appeal is filed, the expiration date of the applicable time to file a notice of appeal from  
24 the Judgment.

25 1.8 “Independent Director” means a member of Kratos’ Board of Directors (the  
26 “Board”) that: (a) has not been employed by the Company or its subsidiaries or affiliates within  
27 the last three calendar years; (b) has not received, during the current calendar year or any of the  
28 three immediately preceding calendar years, remuneration, other than *de minimis* remuneration,

1 as a result of service as or compensation paid to an entity affiliated with an individual who serves  
2 as an advisor, consultant, or legal counsel to the Company or to a member of its senior  
3 management, except for such compensation received in his or her capacity as a director of the  
4 Company;<sup>7</sup> (c) has no personal service contract(s) with the Company, or with any member of its  
5 senior management; (d) is not a current executive officer of a customer of the Company; (e) is not  
6 a director, trustee, or officer with a not-for-profit entity that receives significant contributions  
7 from the Company; (f) during the current calendar year or any of the three immediately preceding  
8 calendar years, has not had any business relationship with the Company for which the Company  
9 has been required to make disclosure under Regulation S-K of the Securities and Exchange  
10 Commission, other than for service as a director or for which relationship no more than *de*  
11 *minimis* remuneration was received in any one such year; provided, however, that the need to  
12 disclose any relationship that existed prior to a director joining the Board shall not in and of itself  
13 render the director non-independent; (g) is not employed by a public company at which an  
14 executive officer of the Company is a member of such other company's compensation committee;  
15 (h) has not had any of the relationships described above, with any controlled affiliate of the  
16 Company; and (i) is not a member of the immediate family of any person who fails to satisfy the  
17 criteria described above.

18 1.9 "Individual Defendants" means Masood Tayebi, Thomas A. Munro, Terry M.  
19 Ashwill, Daniel G. Stokely, Eric Demarco, David A. Garrison, Frankie Farjood, Massih Tayebi,  
20 David Lee, William A. Owens, Bandel L. Carano, James R. Edwards, Scott Fox, Deanna H.  
21 Lund, Andrew M. Leitch, Laura Siegal, Naomi D. Whitacre, William Bradford Weller, George  
22 Wozencraft, and William Mazilly. "Individual Defendants" includes Specially Appearing

23 <sup>7</sup> A director is deemed to have received remuneration (other than as a director, including  
24 remuneration provided to a non-executive Chairman of the Board or Committee Chairman) if  
25 remuneration, other than *de minimis* remuneration, was paid by the Company, its subsidiaries or  
26 affiliates, to any entity, in which the director has a beneficial ownership interest of 5% or more, or  
27 to an entity by which the director is employed or self-employed other than as a director.  
28 Remuneration is deemed *de minimis* if such remuneration is less than \$60,000 in any calendar  
year, or if such remuneration is paid to an entity, it: (i) did not for the calendar year exceed the  
lesser of \$1 million, or 5% of the gross revenues of the entity; and (ii) did not directly result in a  
material increase in the compensation received by the director from that entity.

1 Defendants Farzad Ghassemi, Gregory Jacobsen, Scott I. Anderson, Scot Jarvis, and William  
2 Hoglund.<sup>8</sup>

3 1.10 “Individual Defendant Releasees” means Individual Defendants and each of their  
4 past, present, or future directors, officers, employees, partners, insurers, co-insurers, reinsurers,  
5 principals, agents, controlling shareholders, attorneys, accountants or auditors, advisors,  
6 investment advisors, personal or legal representatives, predecessors, successors, parents,  
7 subsidiaries, divisions, joint ventures, assigns, spouses, heirs, related or affiliated entities,  
8 immediate family, and any trusts in which Individual Defendant Releasees, or any of them, are  
9 the settlors or which are for the benefit of any Individual Defendant Releasees and/or members of  
10 their/his/her immediate family, and any entities in which Individual Defendants, or any of them,  
11 have a controlling interest (directly or indirectly).

12 1.11 “Judgment” means the Final Judgment and Order of Dismissal to be rendered by  
13 the Court, substantially in the form attached hereto as Exhibit A, or as modified pursuant to the  
14 written agreement of the Settling Parties.

15 1.12 “Kratos” or the “Company” means nominal defendant Kratos Defense & Security  
16 Solutions, Inc. (formally known as Wireless Facilities, Inc.), a Delaware corporation with its  
17 principal place of business in San Diego, California, including any of its predecessors, successors,  
18 parents, subsidiaries, divisions, affiliates or related affiliates, and assigns.

19 1.13 “Kratos’ Counsel” means the law firm of Morrison & Foerster LLP.

20 \_\_\_\_\_  
21 <sup>8</sup> In March 2007 and again in February 2008, the Court dismissed Specially Appearing  
22 Defendants Gregory Jacobsen, Farzad Ghassemi, William Hoglund, Scott Anderson, and Scot  
23 Jarvis from the Federal Action for lack of personal jurisdiction. Federal Plaintiffs subsequently  
24 moved the Court, pursuant to Federal Rule of Civil Procedure 54(b), for certification and entry of  
25 final judgment of the Court’s February 2008 Order dismissing the non-residents for lack of  
26 personal jurisdiction. On July 10, 2008, the Court granted Federal Plaintiffs’ motion for  
27 certification. On August 12, 2008, Federal Plaintiffs filed their Notice of Appeal of the February  
28 2008 Order. Due to the ongoing efforts to resolve this matter, and under the direction and  
supervision of the assigned Ninth Circuit mediator, Federal Plaintiffs have not yet filed their  
opening appellate brief. By entering into this Stipulation, the Specially Appearing Defendants do  
not waive, and explicitly reserve, any argument that they might have or that they have made that  
California federal or state courts lack personal jurisdiction over them as to the Derivative Actions  
or any other matter. For purposes of this Stipulation, the Specially Appearing Defendants will  
waive personal jurisdiction for the limited purpose to effectuate the Settlement and Judgment.

1           1.14 “Kratos Releasees,” which does not include Individual Defendant Releasees,  
2 means Kratos and each of its past, present, or future directors, officers, employees, partners,  
3 insurers,<sup>9</sup> co-insurers, reinsurers, principals, agents, controlling shareholders, attorneys,  
4 accountants or auditors, advisors, investment advisors, personal or legal representatives,  
5 predecessors, successors, parents, subsidiaries, divisions, joint ventures, assigns, spouses, heirs,  
6 related or affiliated entities, immediate family, and any trusts in which the Kratos Releasees, or  
7 any of them, are the settlors or which are for the benefit of any Kratos Releasees and/or members  
8 of their/his/her immediate family, and any entities in which Kratos has a controlling interest  
9 (directly or indirectly).

10           1.15 “Kratos Stockholders” means all past or present record and beneficial owners of  
11 Kratos capital stock of all classes and series through the date the Judgment become Final.

12           1.16 “Person” means a natural person, individual, corporation, partnership, limited  
13 partnership, limited liability company, association, joint venture, joint venturer, joint stock  
14 company, estate, legal representative, trust, unincorporated association, government or any  
15 political subdivision or agency thereof, and any business or legal entity and, as applicable,  
16 their/its respective spouses, heirs, executors, administrators, predecessors, successors,  
17 representatives, or assignees.

18           1.17 “Plaintiffs” collectively means Federal Plaintiffs Rosario Pedicini and Michael  
19 Roth, and State Plaintiffs Mary Beth Joseph and Robert Casden, individually and on behalf of  
20 their successors, spouses, heirs, executors, administrators, and assigns, and on behalf of Kratos.

21 \_\_\_\_\_  
22 <sup>9</sup> In April 2009, Kratos commenced litigation against Federal Insurance Company  
23 (“Federal”) for breach of contract, breach of implied warranty, tortious breach of the covenant of  
24 good faith and fair dealing, and declaratory relief — *Kratos Defense & Security, Inc. v. Federal*  
25 *Insurance Co.*, 2:09-cv-03462-FMC-PJWx (C.D. Cal.). That case, which arose out of Federal’s  
26 alleged wrongful refusal to cover defense costs and other losses suffered by Kratos resulting from  
27 several lawsuits and government investigations, including the Derivative Actions, is currently  
28 pending in the United States District Court, Central District of California. Notwithstanding this  
Stipulation, Kratos and its insurance carriers issuing policies for Kratos for the policy period of  
November 3, 2003 to November 3, 2004 do not waive or in any way release Federal, whether  
based on the litigation currently against it or otherwise, or any other insurance carrier issuing  
policies for Kratos for the period of December 3, 2006 to December 3, 2007, for any matter  
whatsoever.

1 1.18 "Plaintiffs' Counsel" means the law firms of Robbins Umeda LLP and Faruqi &  
2 Faruqi, LLP. Plaintiffs' Counsel is Co-Lead Counsel for both State and Federal Plaintiffs in the  
3 Derivative Actions.

4 1.19 "Plaintiff Releasees" means each of Plaintiffs and each of their past, present, or  
5 future directors, officers, employees, partners, insurers, co-insurers, reinsurers, principals, agents,  
6 controlling shareholders, attorneys, accountants or auditors, advisors, investment advisors,  
7 personal or legal representatives, predecessors, successors, parents, subsidiaries, divisions, joint  
8 ventures, assigns, spouses, heirs, related or affiliated entities, immediate family, and any trust of  
9 which any Plaintiff Releasees, or any of them, are the settlors or which is for the benefit of any  
10 Plaintiff Releasees and/or members of their/his/her immediate family, and any entity in which  
11 Plaintiffs, or any of them, have a controlling interest (directly or indirectly).

12 1.20 "Released Claims" means any and all claims or causes of action, demands, rights,  
13 liabilities, suits, debts, obligations, and causes of action of every nature and description  
14 whatsoever, known or unknown (including Unknown Claims as defined herein), contingent or  
15 absolute, mature or unmature, discoverable or undiscoverable, whether concealed or hidden  
16 asserted derivatively on behalf of Kratos, or that could have been asserted directly by the Settling  
17 Parties, derivatively on behalf of Kratos, or by Kratos itself based upon, arising out of, or related  
18 to the allegations, facts, transactions, or claims in the Derivative Actions, and any claims in  
19 connection with, based upon, or arising out of, or relating to the Settlement.

20 1.21 "Settlement" means the terms and conditions set forth in the Stipulation.

21 1.22 "Settling Defendants" means Kratos and each of Individual Defendants.

22 1.23 "Settling Parties" means Kratos, Plaintiffs (on behalf of themselves and Kratos),  
23 and each of Individual Defendants.

24 1.24 "Specially Appearing Defendants" means dismissed defendants Farzad Ghassemi,  
25 Gregory Jacobsen, Scott I. Anderson, Scot Jarvis, and William Hoglund.

26 1.25 "State Plaintiffs" means Mary Beth Joseph and Robert Casden.

27 1.26 "Stipulation" means this Stipulation and Agreement of Settlement of Derivative  
28 Claims, including any recitals and/or exhibits attached hereto.

1           1.27   “Unknown Claims” means any Released Claims that a Person, including Plaintiffs,  
2 may not know or suspect to exist in his, her, or its favor at the time of the release of Kratos and  
3 Individual Defendants which, if known by him, her or it, might have affected his, her, or its  
4 settlement and release, or might have affected his, her, or its decision not to object to this  
5 Settlement. With respect to any and all Released Claims, the Settling Parties stipulate and agree  
6 that, upon the Effective Date, Plaintiffs, Kratos Stockholders, and Kratos shall waive and by  
7 operation of the Judgment shall have waived, the provisions, rights, and benefits of California  
8 Civil Code §1542, which provides:

9           **A GENERAL RELEASE DOES NOT EXTEND TO CLAIMS WHICH THE**  
10           **CREDITOR DOES NOT KNOW OR SUSPECT TO EXIST IN HIS OR HER**  
11           **FAVOR AT THE TIME OF EXECUTING THE RELEASE, WHICH IF**  
12           **KNOWN BY HIM OR HER MUST HAVE MATERIALLY AFFECTED HIS**  
13           **SETTLEMENT WITH THE DEBTOR.**

14           Plaintiffs, Kratos Stockholders, and Kratos shall expressly waive, and by operation of the  
15 Judgment shall have expressly waived, any and all provisions, rights, and benefits conferred by  
16 any law of any state or territory of the United States, or principle of common law, which is  
17 similar, comparable, or equivalent to California Civil Code §1542. Plaintiffs, Kratos  
18 Stockholders, and Kratos may hereafter discover facts in addition to or different from those which  
19 they now know or believe to be true with respect to the Released Claims, but Plaintiffs, Kratos  
20 Stockholders, and Kratos shall expressly fully, finally, and forever settle and release and, upon  
21 the Effective Date, shall be deemed to have, and by operation of the Judgment shall have, fully,  
22 finally, and forever settled and released, any and all Released Claims, known or unknown,  
23 suspected or unsuspected, contingent or non-contingent, whether or not concealed or hidden,  
24 which now exist, or have existed, upon any theory of law or equity now existing or coming into  
25 existence in the future, including, but not limited to, conduct which is negligent, intentional, with  
26 or without malice, or a breach of any duty, law, or rule, without regard to the subsequent  
27 discovery or existence of such different or additional facts. Plaintiffs acknowledge that the  
28 foregoing waiver was separately bargained for and a key element of the Settlement of which this  
release is a part.

1           **2.     Return of Stock Options**

2           In connection with the Settlement of the Derivative Actions, the individuals identified  
3 immediately below agree to provide the following consideration to Kratos within thirty days from  
4 the date the Judgment become Final.

5           2.1     Masood Tayebi and Massih Tayebi agree to forfeit, collectively, a total of 50,000  
6 shares of Kratos stock to Kratos.

7           2.2     Scott I. Anderson agrees to forfeit a total of 2,000 shares of Kratos stock to Kratos.

8           2.3     Scot Jarvis agrees to forfeit a total of 2,000 shares of Kratos stock to Kratos.

9           2.4     Farhad Farjood agrees to forfeit to Kratos any and all claims relating to 10,000  
10 options to purchase shares of Kratos stock.

11          2.5     To the extent that William Bradford Weller still owns or controls any options to  
12 purchase shares of Kratos stock, he agrees to forfeit to Kratos any and all claims relating to  
13 10,000 options to purchase shares of Kratos stock, or all options to purchase shares of Kratos  
14 stock if Mr. Weller holds less than 10,000 options.

15          2.6     To the extent that Thomas Munro still owns or controls any options to purchase  
16 shares of Kratos stock, he agrees to forfeit to Kratos any and all claims relating to 10,000 options  
17 to purchase shares of Kratos stock, or all options to purchase shares of Kratos stock if Mr. Munro  
18 holds less than 10,000 options.

19          2.7     To the extent that Terry Ashwill still owns or controls any options to purchase  
20 shares of Kratos stock, he agrees to forfeit to Kratos any and all claims relating to 10,000 options  
21 to purchase shares of Kratos stock, or all options to purchase shares of Kratos stock if  
22 Mr. Ashwill holds less than 10,000 options.<sup>10</sup>

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23           <sup>10</sup> In negotiating the Settlement, the Settling Parties originally had agreed upon forfeitures  
24 of stock or options to purchase shares of Kratos stock in amounts equal to ten times, respectively,  
25 those amounts enumerated in ¶¶2.1-2.7 herein. In August 2009, however, Kratos announced that  
26 its Board had approved a 1-for-10 reverse split of its common stock, following approval by  
27 Kratos stockholders on June 4, 2009. The record date established for the reverse stock split was  
28 September 10, 2009. Proportional adjustments also were made to Kratos' stock options and other  
equity incentive awards, equity compensation plans, outstanding warrants and convertible notes.  
Accordingly, the amounts of stock or options to purchase shares of Kratos stock set forth in  
¶¶2.1-2.7 herein reflect this 1-for-10 reverse split.

1           **3. Corporate Governance Measures**

2           In full and final settlement of the Derivative Actions, the Kratos Board has agreed to  
3 adopt, or to maintain where already implemented, the corporate governance measures outlined  
4 below within thirty days from the date the Judgment becomes Final and will keep such measures  
5 in force and effect for a period of no less than four years from the date from the date the  
6 Judgment becomes Final, except as stated otherwise in ¶3.10(b) below. Kratos acknowledges that  
7 Plaintiffs' actions, including the institution and prosecution of the Derivative Actions, were a  
8 direct and material factor in the corporate governance policies that have been enacted since the  
9 filing of the Derivative Actions and were a material factor in the enactment of the measures that  
10 will be adopted within thirty days from the date the Judgment becomes Final. The various  
11 measures include:

12           3.1 The Board of Directors

13           (a) The Board shall adopt a resolution that requires all directors, including the  
14 current Board, to attend annually at least one corporate governance class that is designed to keep  
15 corporate directors abreast of trends in governance and aware of their fiduciary, legal, and ethical  
16 responsibilities.

17           (b) The Board shall adopt the appropriate resolutions to implement the  
18 following corporate governance reforms:

19                   (i) the Company's Board shall be increased by two Independent  
20 Directors within eighteen months from the date the Judgment becomes Final;

21                   (ii) each director of the Company shall be elected to the Board by  
22 majority vote;

23                   (iii) no individual member of the Board shall be the Chairman of more  
24 than one Board committee;

25                   (iv) each director of the Company shall be required to certify in writing  
26 annually that he or she has received, read, and understands the guidelines for directors set forth in  
27 the Company's Code of Legal and Ethical Conduct;

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1 (v) the performance of the Chairman of the Board shall be evaluated by  
2 the Board annually. Should the remaining directors determine that the Board Chairman is not  
3 sufficiently active or successful in providing meaningful leadership for the Board, he or she shall  
4 be replaced as the Chairman;

5 (vi) the Company's independent registered public auditing firm may not  
6 perform any consulting work for the Company, other than tax consulting work;

7 (vii) the Company's Chief Executive Officer ("CEO") and Chief  
8 Financial Officer ("CFO") shall be responsible for ensuring that the Company's revenue  
9 recognition policy, which conforms to the requirements of GAAP as currently in effect or as  
10 amended, is implemented and utilized throughout the Company. The CEO and CFO shall report  
11 to the Board on an annual basis regarding the implementation and operation of this policy. The  
12 CEO and CFO shall distribute the Company's revenue recognition policy to each such Company  
13 employee who records or reviews the recording of revenue and ensure that each such Company  
14 employee completes an employee training program concerning the Company's policy on revenue  
15 recognition. Any questions regarding that policy or training program, or the application of the  
16 policy, shall be directed to the Company's CFO, who shall inform the CEO; and

17 (viii) at each regularly scheduled Board meeting, the Company's CFO (or  
18 his or her designee) shall provide a report as to the Company's financial condition and prospects,  
19 including, but not limited to, a discussion of any material decreases in revenues and earnings, if  
20 any, management plans for ameliorating or reversing such negative trends and the success or  
21 failure of any such plans presented in the past.

22 3.2 Responsibilities of the Independent Directors

23 (a) The Board shall adopt a resolution requiring that a majority of the members  
24 of the Board shall be Independent Directors.

25 (b) The Independent Directors shall meet separately from the rest of the Board  
26 on a quarterly basis.

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3.3 Board Committees

(a) The Board will re-institute its Nominating and Corporate Governance Committees consisting of no less than two Independent Directors to oversee the nomination of the additional director(s), and to implement and oversee appropriate corporate governance reforms.

(b) The Board's committees shall have standing authorization, in their own discretion, to retain legal or other advisors of their choice, who shall report directly to the Board or committee.

(c) The Bylaws of the Company shall be revised to include specific limits on outside board memberships. The CEO of the Company shall not participate on the board of directors of any more than one additional for-profit corporation (either publicly traded or privately held) for a period of two years,<sup>11</sup> and a majority of Independent Directors shall not serve on more than three boards of directors of publicly held companies, including the Company. Any CEO or other full-time senior corporate officer of another company serving on the Company's Board shall be limited to not more than two public company boards of directors in total, including the boards of directors of such person's own employer and the Company.

3.4 Compensation Committee

(a) The Company shall have a Compensation Committee Charter that expressly vests in the Compensation Committee the responsibility and obligation to:

(i) approve the Company's stock option grants, including the approval of employees and parties who are to receive stock option grants and the details of those option grants; and

(ii) prevent the granting, issuance, or approval of any stock options that have been or can be market-timed, backdated, or otherwise manipulated.

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<sup>11</sup> The CEO will be permitted to serve on the board of directors of not more than one additional company with advance consent of the Nominating and Corporate Governance Committee. In general, however, the CEO shall devote his or her full energies to running the Company.

1 (b) The Compensation Discussion and Analysis written for the Company's  
2 annual Proxy Statement shall address efforts undertaken by the Compensation Committee to  
3 design and implement systems and controls to prevent the granting, issuance, and/or approval of  
4 market-timed, backdated, or manipulated stock option grants.

5 (c) The Compensation Committee shall not delegate its authority to grant stock  
6 options to a Stock Option Administrator unless the delegated Stock Option Administrator is a  
7 member of the Compensation Committee of the Board. If a Stock Option Administrator is  
8 delegated the authority to grant stock options, any stock option grant by the Stock Option  
9 Administrator must be approved by the entire Compensation Committee.

10 (d) The Compensation Committee shall select and retain an independent  
11 compensation consultant to provide advice and guidance to the Committee as needed. In  
12 addition, the consultant shall, at such times as requested by the Committee, conduct a  
13 comparative market study of the Company's executive compensation policies, practices, and  
14 procedures. This study shall be delivered to the Compensation Committee for its use in  
15 evaluating and revising, if necessary, the compensation structure for the Company's executives.

16 3.5 Enhanced Internal Audit Function

17 (a) The Company shall implement and maintain an enhanced internal audit  
18 function. The Company's outside auditor shall not provide this service. The Internal Auditor,  
19 who shall be approved by the Board and report directly to the Audit Committee at least annually,  
20 shall review the Company's internal control environment. The Internal Auditor shall be  
21 responsible for devising an Internal Audit Plan for each fiscal year that will be presented to the  
22 Audit Committee.

23 (b) A written report shall be prepared for each internal audit performed  
24 describing the internal audit's findings, opinions, and recommendations, if any. These written  
25 reports shall be directed to the CEO, CFO, and the Audit Committee for review and, if necessary,  
26 remedial action.

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1           3.6    Audit Committee

2                   (a)    The Audit Committee shall use its best efforts to have at least two members  
3 with an accounting or financial management background. If an Audit Committee member  
4 possessing such accounting or financial background resigns, is terminated, or otherwise is  
5 removed from his or her directorship on the Audit Committee, the Board shall use its best efforts  
6 to replace such director within ninety days of his or her departure with another director that has an  
7 accounting or financial management background. These best efforts shall include the  
8 commencement of a search to locate an additional Board member with an accounting or financial  
9 management background.

10                   (b)    The Audit Committee shall have a charter which includes the following  
11 provisions:

12                           (i)    meetings to be held, among other times, prior to the commencement  
13 and prior to the completion of the annual audit;

14                           (ii)   each meeting shall include a meeting with appropriate Company  
15 management, followed by an executive session with no management present; and

16                           (iii)   each meeting shall have a written agenda.

17                   (c)    The Audit Committee’s responsibilities shall include:

18                           (i)    meeting with the Company’s independent registered public  
19 accounting firm concerning:

20                                   (1)    the reliability of the Company’s forward-looking statements  
21 contained in interviews with media agencies, investor conference calls, committee reports,  
22 quarterly and annual reports, proxy statements, and press releases disseminated by the Company;  
23 and

24                                   (2)    the reliability of the Company’s statements relating to  
25 internal financial control mechanisms contained in interviews with media agencies, investor  
26 conference calls, committee reports, quarterly and annual reports, proxy statements, and press  
27 releases disseminated by the Company.  
28

1 (ii) meeting with management to ascertain the Company's primary  
2 business exposure risks; and

3 (iii) meeting with the Company's Internal Auditors at year-end  
4 regarding:

5 (1) the nature of the internal audit plan, including the  
6 effectiveness and continued use of the policies and procedures of the internal audit plan;

7 (2) the appropriate staffing levels for the internal audit function;

8 (3) whether the Company's financial reporting policies and  
9 practices are sufficiently transparent; and

10 (4) whether the Company's financial reporting policies and  
11 practices are unusually aggressive.

12 3.7 Stock Option Granting Policies and Procedures

13 (a) The following stock-option related controls, that already have been  
14 implemented by the Company, will be maintained for a period of no less than four years from the  
15 date of entry of the Judgment:

16 (i) segregating certain responsibilities related to option granting and  
17 the execution of stock option exercise transactions, including, but not limited to, the Director of  
18 Financial Reporting being required to approve exercises and the Assistant Controller/Director of  
19 Financial Reporting being required to separately review all entries to the Company's Equity Edge  
20 database by the Stock Option Administrator;

21 (ii) documenting and assessing the design and operating effectiveness  
22 of key internal controls over the stock administration function;

23 (iii) establishing processes and procedures to increase communications  
24 between the stock administration, human resources, and accounting functions, including but not  
25 limited to, requiring communications between human resources and accounting/finance related to  
26 any separation agreement that might result in a modification of terms;

27 (iv) adding independent reviews and reconciliations of stock option  
28 activity separate from the stock administration function;

1 (v) establishing a consistent, formalized procedure for stock option  
2 award procedures including limiting the authority to approve stock option grants;

3 (vi) upgrading the equity tracking software program and system  
4 controls that support the processes and continuing to maintain the most current version of the  
5 option tracking software;

6 (vii) requiring and arranging for training for those employees who utilize  
7 the Company's equity tracking software program, as well as all those involved in the stock option  
8 granting process, to enhance awareness and understanding of legal, tax, and accounting  
9 implications;

10 (viii) requiring that only an employee independent of the stock  
11 administration function be allowed to communicate stock option exercise instructions to the  
12 Company's transfer agent;

13 (ix) requiring quarterly reconciliation of exercises according to transfer  
14 agent records versus exercises according to the Equity Edge database to identify any  
15 discrepancies;

16 (x) requiring approval by the Company's Compensation Committee  
17 during meetings rather than by use of Unanimous Written Consents;

18 (xi) requiring the development of an annual option granting plan and  
19 option granting matrix;

20 (xii) dissolving the Company's non-officer stock option committee; and

21 (xiii) the grant date of all stock options shall be the fifteenth trading day  
22 of the month after which they are approved.

23 (b) All stock option plans adopted by the Company shall clearly define the  
24 exercise price, grant date, and the fair market value of stock. The exercise price or value of any  
25 equity award shall be determined by fair market value of the Company's stock on the date of the  
26 grant. The fair market value of the Company's stock shall be the closing price (or closing bid, if  
27 no sales were reported) for a share of the Company's stock on such days as quoted by the  
28 exchange or over-the-counter market on which the stock is listed.

1 (c) Any and all stock option plans that permit market timing or backdating of  
2 stock options are void and shall be without force or effect.

3 (d) Any substitute stock option plan(s) adopted by the Company in the future  
4 must expressly prohibit market timing and backdating of stock options.

5 (e) Any stock option plans shall give the Compensation Committee the sole  
6 and exclusive power and duty to administer the Company's stock option plans.

7 (f) Any and all disclosure requirements concerning executive compensation  
8 and stock option grants, including the Sarbanes-Oxley Act of 2002 disclosure requirements, shall  
9 be followed by the Company.

10 (g) All requirements of the Internal Revenue Code as they relate to the  
11 granting, issuance, timing, pricing, and treatment of stock options shall be observed and followed  
12 by the Company.

13 (h) The substance of the following clauses shall be included in any current  
14 and/or subsequent equity incentive plan, whether subject to stockholder approval or not:

15 (i) The exercise price for each stock option grant shall be at least 100%  
16 of the fair market value on the date of the grant;

17 (ii) the Company shall give notice of the determination to each  
18 employee or consultant to whom a stock option is so granted as soon as reasonably practicable,  
19 but in no event shall such notice be given more than thirty days after the date of such grant; and

20 (iii) authority to grant stock option awards shall be limited to the full  
21 Board or the Compensation Committee, consisting of three or more independent directors, and  
22 shall not be delegated to any other person or body.

23 3.8 Insider Trading Policy

24 The Company shall adopt an Insider Trading Policy that provides as follows:

25 (a) The Insider Trading Policy shall specifically prohibit all Company  
26 directors, officers and employees from trading in Company securities while in possession of  
27 material, non-public information regarding the Company, including, but not limited to:

28 (i) material, non-public information regarding actual or estimated results of operations and

1 earnings; (ii) material, non-public proposals or agreements relating to mergers, acquisitions or  
2 divestitures; and (iii) material, non-public information regarding significant contracts, patents, or  
3 new product development.

4 (b) The Insider Trading Policy shall encourage all directors and Section 16  
5 officers who wish to trade in Company securities to adopt a valid trading plan pursuant to SEC  
6 Rule 10b5-1, 17 C.F.R. § 240.10b5-1.

7 (c) The Insider Trading Policy shall require all other Company employees who  
8 wish to trade in Company securities to do so only within prescribed trading windows, to be  
9 established by the Board. All Company employees who have not adopted a valid Rule 10b5-1  
10 trading plan shall be prohibited from trading in Company securities, except during open trading  
11 windows.

12 3.9 Related-Party Transactions

13 (a) The Company shall maintain its policy entitled “Conflict of Interest and  
14 Related Party Transactions,” which became effective on October 9, 2007.

15 (b) Any material changes to the Conflict of Interest and Related Party  
16 Transactions Policy may be made only with the approval of the Board.

17 3.10 Additional Controls

18 (a) The following additional controls that already have been implemented by  
19 the Company will be maintained for a period of no less than four years from the date of entry of  
20 the Judgment:

21 (i) The Company shall continue to maintain its internal Contracts  
22 Administration Department, which has been established to ensure that complete contract files are  
23 maintained to support the project estimate-at-completion computation. This is accomplished  
24 using a database in which all relevant contract administration documents are maintained. As a  
25 part of the revised revenue recognition procedures, the database is accessed to update information  
26 needed in the period-end estimate-at-completion.

27 (ii) In conjunction with the Company’s month-end and year-end  
28 closing procedures, the Company has implemented additional monitoring and review controls

1 over its estimate-at-completion calculations, as well as its invoicing/customer billings procedures  
2 and its valuation of accounts receivable balances.

3 (iii) Shareholder Nominated Director Process. The Independent  
4 Directors shall consider and evaluate recommendations for director nominees proposed by a  
5 qualified stockholder. The stockholder must submit its director nominee recommendation to the  
6 Corporate Secretary in writing and provide the following information:

7 (1) a statement by the stockholder that: (i) the stockholder is  
8 the holder of at least 1% of the Company's capital stock; (ii) the stock has been held for at least  
9 one year prior to the date of the submission; and (iii) the stockholder will continue to hold the  
10 shares through the date of the annual stockholder meeting;

11 (2) the candidate's name, age, contact information, and current  
12 principal occupation or employment;

13 (3) a description of the candidate's qualifications and business  
14 experience during, at a minimum, the last five years, including the candidate's principal  
15 occupation or employment, and the name and principal business of any corporation or other  
16 organization in which the candidate was employed;

17 (4) the candidate's resume; and

18 (5) three references.

19 (iv) to be evaluated in connection with the Company's established  
20 procedures for evaluating potential director nominees, the qualifying stockholder must provide  
21 the stockholder's director nominee recommendation to the Company at least 120 days prior to the  
22 anniversary of the date proxy statements were mailed to stockholders in connection with the prior  
23 year's annual stockholder meeting.

24 (b) The Chairman of the Board must not simultaneously hold the position of  
25 CEO. Given the importance of finding an appropriate Chairman of the Board, the Company will  
26 have four years from the date the Judgment becomes Final to begin complying with this  
27 provision. This provision shall remain in effect for a period of no less than four years from the  
28 date on which the provision is first implemented.

1           **4.     Restriction of Voting Rights**

2           In connection with the Settlement of the Derivative Actions, Masood Tayebi and Massih  
3           Tayebi hereby agree that for a period of no less than three years from the date the Judgment  
4           becomes Final, they will not exercise any of the voting rights associated with any of the shares of  
5           Kratos stock that they personally own or that they control through any trust or other entity.  
6           Masood Tayebi and Massih Tayebi shall provide the Company with a signed certification each  
7           year stating that they did not exercise any of the voting rights associated with any of the shares  
8           they own or control and did not make any material recommendations to anyone exercising voting  
9           rights in Kratos stock with respect to the exercise of those rights.

10           **5.     Attorneys' Fees and Reimbursement of Expenses**

11           5.1     Subject to Court approval and in recognition of the benefits conferred on Kratos as  
12           a direct and material factor resulting from the Derivative Actions, Kratos agrees to pay and/or to  
13           cause its D&O Insurer(s) to pay to Plaintiffs' Counsel \$2,000,000, based upon an agreement  
14           reached between and among Kratos and its D&O Insurer(s) concurrently with this Settlement, for  
15           Plaintiffs' Counsel's attorneys' fees and reimbursement of expenses. Kratos also agrees to cause  
16           its D&O Insurer(s) to pay to Kratos a substantial portion of past and anticipated future legal fees  
17           and related costs, incurred by Defendants' counsel in connection with the Derivative Actions  
18           based upon a separate agreement reached between and among Kratos and its D&O Insurer(s)  
19           concurrently with this Settlement. Plaintiffs' Counsel shall not seek a fee in excess of \$2,000,000  
20           and Kratos will not oppose a fee request by Plaintiffs' Counsel of \$2,000,000. Kratos shall cause  
21           to be transferred to an account maintained by Plaintiffs' Counsel \$2,000,000 within five business  
22           days of entry of the order preliminarily approving the Settlement and providing for notice to  
23           Current Kratos Stockholders of the hearing on this Settlement. The Fees and Expenses Payment  
24           is subject to the obligation of Plaintiffs' Counsel and their law firms (or their successors) to  
25           refund that amount plus interest thereon at the then-current ninety-day T-Bill rate, in the event of  
26           a reversal or modification on appeal or if the Effective Date does not occur. Said refund shall be  
27           paid to Kratos within ten business days of written notification of that event.

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1           5.2     In the event the Stipulation shall terminate, or be canceled, or shall not become  
2 effective for any reason, or if the Judgment or the order awarding fees and expenses is reversed or  
3 modified on appeal, within ten business days after written notification of such event is sent by  
4 Kratos' Counsel to Plaintiffs' Counsel, the Fees and Expenses Payment (including any accrued  
5 interest), or portion thereof, shall be refunded by Plaintiffs' Counsel to Kratos in an amount  
6 consistent with such reversal or modification. Plaintiffs' Counsel, as a condition of receiving  
7 such fees and reimbursement of expenses, on behalf of itself and each of its partners and/or  
8 shareholders, agrees that the law firm and its partners and/or shareholders are subject to the  
9 jurisdiction of the Court for the purpose of enforcing the Stipulation. Without limitation, each  
10 such law firm and its partners and/or shareholders agree that the Court may, upon application of  
11 Kratos or Individual Defendants and on notice to Plaintiffs' Counsel, summarily issue orders,  
12 including but not limited to, judgments and attachment orders, and may make appropriate  
13 findings of or sanctions for contempt, against them or any of them should such law firm fail to  
14 timely repay the Fees and Expenses Payment it received.

15           5.3     Plaintiffs' Counsel shall have sole responsibility for apportioning and distributing  
16 the Fees and Expenses Payment, and in no event shall Individual Defendants or Kratos have any  
17 obligations or liability with respect to that apportionment or distribution, and/or to any Person  
18 who may assert some claim thereto.

19           5.4     Any order or proceedings relating to the Fees and Expenses Payment, or any  
20 appeal from any order relating thereto or reversal or modification thereof, shall not operate to  
21 terminate, modify or cancel the Stipulation, or affect or delay the finality of the Judgment  
22 approving the Stipulation and the settlement of the Action.

23           5.5     Except as expressly provided for in ¶¶5.1-5.3 above, Plaintiffs and Plaintiffs'  
24 Counsel shall bear their own attorneys' fees and costs incurred in connection with the matters set  
25 forth in this Stipulation.

## 26           **6. Preliminary Approval, Notice Orders, and Settlement Hearing**

27           6.1     Within thirty calendar days after the execution of this Stipulation, counsel for the  
28 Settling Parties, or any of them, shall submit this Stipulation together with its Exhibits to the

1 Court and shall apply for entry of an order, substantially in the form of Exhibit B attached hereto,  
2 preliminarily approving the Settlement set forth in the Stipulation, and providing for notice of  
3 Current Kratos Stockholders of the hearing on this Settlement (the “Preliminary Approval  
4 Order”). Such order shall specifically include provisions that will:

5 (a) preliminarily approve this Stipulation and the Settlement set forth herein;

6 (b) approve the Summary Notice of Pendency and Settlement of Derivative  
7 Actions (the “Summary Notice”), substantially in the form of Exhibit B-1 attached hereto, for  
8 publication in a national financial newspaper, such as *Investor’s Business Daily*, and a nationally  
9 recognized newswire, such as PR Newswire;

10 (c) approve the Notice of Pendency and Settlement of Derivative Actions (the  
11 “Notice”), substantially in the form of Exhibit B-2 attached hereto, for posting on the websites of  
12 Kratos and Robbins Umeda LLP, and for filing by Kratos with the SEC via a Form 8-K;

13 (d) find that the Notice and Summary Notice given pursuant to subparagraph  
14 (b) above constitutes the best notice practicable under the circumstances and is valid, due, and  
15 sufficient notice to all such Persons under California and/or Delaware law, the United States  
16 Constitution, and any other applicable law;

17 (e) schedule a hearing (the “Settlement Hearing”) to be held by the Court to  
18 determine whether the proposed Settlement as contained in this Stipulation should be approved as  
19 fair, just, reasonable, and adequate and the Judgment approving the Settlement should be entered;

20 (f) provide that any objections by Current Kratos Stockholders to: (i) the  
21 proposed Settlement contained in this Stipulation, or (ii) the entry of the Judgment approving the  
22 Settlement shall be heard, and any papers submitted in support of said objections shall be  
23 received and considered by the Court at the hearing only if, on or before a date to specified in the  
24 Notice, Persons making objections file notice of their intention to appear and copies of any papers  
25 in support of their position with the Clerk of the Court and serve such notice and papers on  
26 counsel as identified in the Notice;

27 (g) provide that pending final determination of whether the Settlement  
28 contained in this Stipulation should be approved, neither Plaintiffs, nor any Kratos Stockholder,

1 either directly, representatively, derivatively, or in any other capacity, shall commence or  
2 prosecute any action or proceeding in any court or tribunal asserting any of the claims released in  
3 this Stipulation against Settling Defendants;

4 (h) provide that the Settlement Hearing may, from time to time and without  
5 further notice to the Current Kratos Stockholders, be continued or adjourned by order of the  
6 Court;

7 (i) provide that Kratos shall be solely responsible for, and shall cause to be  
8 paid, the cost of printing and dissemination of the Notice.

9 **7. Releases and Bar**

10 7.1 Upon the Effective Date, Plaintiffs, on behalf of themselves and, to the fullest  
11 extent permitted by law, on behalf of Kratos Stockholders, shall be deemed to have, and by  
12 operation of the Judgment shall have, fully, finally, and forever released, relinquished, and  
13 discharged all Released Claims (including Unknown Claims), and any and all claims relating to  
14 or arising out of or connected with the Settlement or resolution of the Derivative Actions, against  
15 Individual Defendant Releasees and Kratos Releasees, except for obligations imposed by the  
16 Stipulation in connection with the Settlement.

17 7.2 Upon the Effective Date, Kratos and the Individual Defendants shall be deemed to  
18 have, and by operation of the Judgment shall have, fully, finally, and forever released,  
19 relinquished, and discharged Plaintiff Releasees from all claims (including Unknown Claims),  
20 arising out of, based upon or related to the institution, prosecution, assertion, settlement, or  
21 resolution of the Derivative Actions and/or the Released Claims, except for obligations imposed  
22 by the Stipulation in connection with the Settlement.

23 7.3 Upon the Effective Date, each of the Individual Defendants shall be deemed to  
24 have, and by operation of the Judgment shall have, fully, finally, and forever released,  
25 relinquished, and discharged Kratos Releasees from all claims (including all Unknown Claims)  
26 arising out of, based upon or related to the institution, prosecution, assertion, settlement, or  
27 resolution of the Derivative Actions, except that the Individual Defendants, by virtue of this  
28 Stipulation, have not released, relinquished, or discharged Kratos Releasees from any rights,

1 claims, or causes of action for indemnification, including, but not limited to, insurance  
2 indemnification, and/or advancement of attorneys' fees and expenses (or other defense costs), for  
3 any matter whatsoever, required or permitted to the fullest extent under Kratos' Certificate of  
4 Incorporation or Bylaws, California or Delaware law, or any indemnification or similar  
5 agreement between Kratos and any such Individual Defendants.

6 7.4 Upon the Effective Date, Kratos shall be deemed to have, and by operation of the  
7 Judgment shall have, fully, finally, and forever released, relinquished, and discharged all  
8 Released Claims (including Unknown Claims), and any and all claims relating to or arising out of  
9 or connected with the Settlement or resolution of the Derivative Actions, against the Individual  
10 Defendant Releasees.

11 7.5 Upon the Effective Date, each of the Individual Defendants shall be deemed to  
12 have, and by operation of the Judgment shall have, fully, finally, and forever released,  
13 relinquished, and discharged all Released Claims (including Unknown Claims), and any and all  
14 claims relating to or arising out of or connected with the Settlement or resolution of the  
15 Derivative Actions against the other Individual Defendant Releasees, except that Individual  
16 Defendants by virtue of this Stipulation have not released, relinquished, or discharged Kratos  
17 Releasees from any rights, claims, or causes of action for indemnification, including, but not  
18 limited to, insurance indemnification, and/or advancement of attorneys' fees and expenses (or  
19 other defense costs), for any matter whatsoever required or permitted to the fullest extent under  
20 Kratos' Certificate of Incorporation or Bylaws, California or Delaware law, or any  
21 indemnification or similar agreement between Kratos Releasees and any such Individual  
22 Defendants.

23 7.6 Pending final determination of whether the Settlement should be approved, neither  
24 Plaintiffs, Kratos, nor any Kratos Stockholders shall commence, maintain, or prosecute against  
25 any of Settling Defendants, whether directly or derivatively on behalf of Kratos, any action or  
26 proceeding in any court or tribunal asserting any of the Released Claims, and all proceedings and  
27 further activity between the Settling Parties in the Derivative Actions, except for those activities  
28 and proceedings relating to the Stipulation and the Settlement, shall be stayed.

1           **8.     Effective Date and Conditions of Settlement**

2           8.1     The Effective Date shall be the first date by which all the following events and  
3 conditions shall have occurred or been met:

- 4                   (a)     execution of the Stipulation;
- 5                   (b)     entry of the Preliminary Approval Order;
- 6                   (c)     entry of the Judgment;
- 7                   (d)     payment of Plaintiffs' Counsel's attorneys' fees and reimbursement of  
8 expenses in accordance with ¶5.1;
- 9                   (e)     the Judgment has become Final; and
- 10                  (f)     dismissal of the State Action with prejudice in accordance with ¶8.4.

11           8.2     If all of the conditions specified in ¶8.1 are not met, then this Stipulation shall be  
12 canceled and terminated, and the Fees and Expenses Payment (plus any interest that has accrued  
13 thereon) shall be returned subject to ¶5.2, unless Plaintiffs' Counsel, counsel for the Individual  
14 Defendants, and Kratos' Counsel mutually agree in writing to waive or modify any conditions  
15 that are not satisfied and otherwise agree to proceed with this Stipulation.

16           8.3     In the event that the Stipulation or Settlement is not approved by the Court, the  
17 State Action is not dismissed with prejudice, or the Settlement set forth in the Stipulation is  
18 terminated for any reason, the Settling Parties shall be restored to their respective positions in the  
19 Derivative Actions as of January 5, 2010, and all negotiations, proceedings, documents prepared,  
20 and statements made in connection herewith shall be without prejudice to the Settling Parties,  
21 shall not be deemed or construed to be an admission by any Settling Party of any act, matter, or  
22 proposition and shall not be used in any manner or for any purpose in any subsequent proceeding  
23 in the Derivative Actions or in any other action or proceeding. In such event, the terms and  
24 provisions of the Stipulation, with the exception of ¶¶5.2, 6.1(i), 8.2-8.3, 10.1-10.16 herein, shall  
25 have no further force and effect with respect to the Settling Parties and shall not be used in the  
26 Derivative Actions or in any other proceeding for any purpose, and any Judgment or order  
27 entered by the Court in accordance with the terms of the Stipulation shall be treated as vacated,  
28 *nunc pro tunc*.

1           8.4     Within five business days from the date on which the Judgment becomes Final,  
2 Plaintiffs' Counsel, on behalf of State Plaintiffs, shall file a Stipulation of Dismissal with  
3 prejudice in the State Action, signed by all parties to the State Action, and request an order  
4 dismissing the State Action. Plaintiffs' Counsel, on behalf of State Plaintiffs, shall file and serve  
5 notice of any dismissal order within five business days of entry by the State Court.

6           **9.     Bankruptcy**

7           9.1     In the event that a case is commenced in respect to any Individual Defendant or  
8 Kratos under Title 11 of the United States Code (Bankruptcy), or a trustee, receiver, or  
9 conservator is appointed under any similar law, the Settling Parties agree to use their reasonable  
10 best efforts to obtain all necessary orders, consents, releases, and approvals for effectuation of this  
11 Stipulation in a timely and expeditious manner. By way of example only, the Settling Parties  
12 agree to cooperate in making applications and motions to the bankruptcy court for relief from any  
13 stay, approval of the settlement, authority to release funds, authority for Kratos' insurer to  
14 disburse insurance proceeds consistent with this Stipulation, authority to release claims and  
15 indemnify officers and directors, and authority for the Court to enter all necessary orders and  
16 judgments, and any other actions reasonably necessary to effectuate the terms of this Stipulation.

17           9.2     In the event that a case is commenced in respect to any Individual Defendant or  
18 Kratos under Title 11 of the United States Code (Bankruptcy), or a trustee, receiver, or  
19 conservator is appointed under any similar law, the Settling Parties agree that all dates and  
20 deadlines set forth herein will be extended for such periods of time as are necessary to obtain  
21 necessary orders, consents, releases, and approvals from the bankruptcy court for effectuation of  
22 this Stipulation.

23           **10.    Miscellaneous Provisions**

24           10.1     The Settling Parties (a) acknowledge that it is their intent to consummate this  
25 Settlement; and (b) agree to cooperate to the extent necessary to effectuate and implement all  
26 terms and conditions of the Stipulation and to exercise their reasonable best efforts to accomplish  
27 the foregoing terms and conditions of the Stipulation.  
28

1           10.2   Except as to any existing obligation of Kratos to the Individual Defendants, the  
2   Settling Parties intend this Settlement to be a final and complete resolution of all disputes  
3   between them with respect to the claims made in the Derivative Actions.

4           10.3   Neither this Stipulation nor the Settlement contained herein, nor any act performed  
5   or document executed pursuant to or in furtherance of the Stipulation or the Settlement: (a) is or  
6   may be deemed to be or may be used as an admission of, or evidence of, the validity of any  
7   claims released therein or by virtue of the releases attached thereto, including any of the Released  
8   Claims; or (b) may be deemed to be or may be used as an admission or evidence of any fault,  
9   wrongdoing, omission, or liability of any of the Settling Defendants, in any civil, criminal, or  
10   administrative proceeding in any court, administrative agency or other tribunal. Settling  
11   Defendants may file the Stipulation, the Judgment, and/or any document executed pursuant to or  
12   in furtherance of the Stipulation, in any action that may be brought against them in order to  
13   support a defense or counterclaim based on principles of *res judicata*, collateral estoppel, full  
14   faith and credit, release, judgment bar reduction, or any theory of claim preclusion or issue  
15   preclusion or similar defense or counterclaim. The Individual Defendants have denied and  
16   continue to deny each and all of the claims alleged or threatened or suggested against them in or  
17   relating to the Derivative Actions. While Individual Defendants deny that the claims advanced in  
18   the Derivative Actions were meritorious, Individual Defendants agree and the Judgment in the  
19   Federal Action will state, that the Derivative Actions were filed in good faith and in accordance  
20   with the applicable California and/or Delaware law and the Federal Rules of Civil Procedure,  
21   including Rule 11 of the Federal Rules of Civil Procedure, and are being settled voluntarily after  
22   consultation with competent legal counsel.

23           10.4   In the event that any part of the Settlement is found to be unlawful, void,  
24   unconscionable, or against public policy by a court of competent jurisdiction, the Settling Parties  
25   agree that the remaining terms and conditions of the Settlement shall remain intact. Further, the  
26   waiver by one party of any breach of this Stipulation by any other party shall not be deemed a  
27   waiver of any other prior or subsequent breach of this Stipulation.  
28

1           10.5    The Settling Parties, and each of them, agree, to the extent permitted by law, that  
2 all agreements made and orders entered during the course of the Derivative Actions relating to the  
3 confidentiality of information shall survive this Stipulation.

4           10.6    All confidential discovery materials produced during the Derivative Actions shall,  
5 within thirty days after the Effective Date, be destroyed by the party obtaining the materials,  
6 provided, however, that counsel's work product need not be destroyed. A letter certifying  
7 compliance with this provision shall be provided to counsel for the producing party.

8           10.7    The Exhibits attached hereto are material and integral parts hereof and are hereby  
9 incorporated by reference as though fully set forth herein.

10          10.8    The Stipulation may be amended or modified only by a written instrument signed  
11 by or on behalf of all Settling Parties or their successors-in-interest.

12          10.9    Each counsel or other person executing the Stipulation or its Exhibits on behalf of  
13 any Settling Party hereto warrants that such person has the full authority to do so and are  
14 expressly authorized by their client(s) to take all appropriate action required or permitted to be  
15 taken pursuant to the Stipulation to effectuate its terms and also are expressly authorized to enter  
16 into any modifications or amendments to the Stipulation on behalf of their client(s) that they  
17 deem appropriate.

18          10.10   Except as provided herein, the Stipulation and the Exhibits attached hereto  
19 constitute the entire agreement among the Settling Parties, and no representations, warranties or  
20 inducements have been made to any Settling Party concerning the Stipulation or its Exhibits other  
21 than the representations, warranties and covenants contained and memorialized in such  
22 documents.

23          10.11   The headings herein are used for the purpose of convenience only and are not  
24 meant to have legal effect.

25          10.12   The Court shall retain jurisdiction with respect to implementation and enforcement  
26 of the Stipulation, and all parties hereto submit to the jurisdiction of the Court for purposes of  
27 implementing and enforcing the Settlement.

28

1           10.13 The Stipulation may be executed in one or more counterparts. All executed  
2 counterparts and each of them shall be deemed to be one and the same instrument. Counsel for  
3 the Settling Parties to the Stipulation shall exchange among themselves signed counterparts, and a  
4 complete set of original executed counterparts shall be filed with the Court.

5           10.14 The Stipulation shall be binding upon, and inure to the benefit of, the successors  
6 and assigns of the Settling Parties hereto. Plaintiffs and Plaintiffs' Counsel represent and warrant  
7 that none of the claims or causes of action asserted by them, or that could have been asserted by  
8 them, in the Derivative Actions have been assigned, encumbered, or in any manner transferred, in  
9 whole or in part.

10           10.15 The Stipulation and the Exhibits thereto shall be considered to have been  
11 negotiated, executed, and delivered, and to be wholly performed, in the State of California, and  
12 the rights and obligations of the parties to the Stipulation, and the construction, interpretation,  
13 operation, effect, and validity of this Stipulation, and all documents necessary to effectuate it,  
14 shall be governed by the internal laws of the State of California without regard to conflict of law  
15 principles.

16           10.16 This Stipulation shall not be construed more strictly against one party than another  
17 merely by virtue of the fact that it, or any part of it, may have been prepared by counsel for one of  
18 the parties, it being recognized that it is the result of arm's-length negotiations between the parties  
19 and all parties have contributed substantially and materially to the preparation of this Stipulation.

20           IN WITNESS WHEREOF, the Settling Parties hereto have caused the Stipulation to be  
21 executed, by their duly authorized attorneys.

22 Dated: January 5, 2010

MORRISON & FOERSTER LLP

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By:           s/Sean T. Prosser          

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Dated: January 5, 2010

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Dated: January 5, 2010

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Dated: January 5, 2010

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**CERTIFICATE OF SERVICE**

I hereby certify that on January 8, 2010, the foregoing document was filed with the Clerk of the Court for the U.S. District Court, using the electronic case filing system of the court. The electronic case filing system sent a "Notice of Electronic Filing" to all attorneys of record who have consented in writing to accept this Notice as service of documents by electronic means. I hereby certify that I have served the foregoing document to all individuals who have not consented to electronic notification by mail, and to counsel not on the Court's list to receive e-mail notices, as indicated in the attached service list.

\_\_\_\_\_  
s/Brian J. Robbins

BRIAN J. ROBBINS

## Mailing Information for a Case 3:04-cv-01663-JAH-NLS

### Electronic Mail Notice List

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### Manual Notice List

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- (No manual recipients)

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UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF CALIFORNIA

IN RE WIRELESS FACILITIES, INC.,  
DERIVATIVE LITIGATION

Case No. 04-CV-1663 JAH (NLS)  
**[PROPOSED] FINAL JUDGMENT  
AND ORDER OF DISMISSAL**

\_\_\_\_\_  
This Document Relates to:  
**ALL ACTIONS.**

**EXHIBIT A**

This matter came before the Court for hearing pursuant to the Order of this Court, dated \_\_\_\_\_, 2010, on the application of the parties for approval of the Settlement set forth in the Stipulation and Agreement of Settlement of Derivative Claims dated as of January 5, 2010, and the Exhibits thereto (the “Stipulation”). Due and adequate notice having been given to stockholders of Kratos Defense & Security Solutions, Inc. (formerly known as Wireless Facilities, Inc.) (“Kratos”), as required in said Order, and the Court having considered all objections raised, if any, and having considered all arguments made and papers filed and proceedings had herein, and otherwise being fully informed and good cause appearing therefore, **IT IS HEREBY ORDERED, ADJUDGED, AND DECREED** that:

1. For purposes of this Final Judgment and Order of Dismissal (the “Judgment”), the Court incorporates by reference the definitions in the Stipulation, and all capitalized terms used herein shall have the same meanings as set forth in the Stipulation.

1           2.       This Court has jurisdiction over the subject matter of the above-captioned Federal  
2 Action, including all matters necessary to effectuate the Settlement, and over all Settling Parties,  
3 including nominal defendant Kratos.<sup>1</sup>

4           3.       Pursuant to Rule 23.1 of the Federal Rules of Civil Procedure, this Court hereby  
5 approves the Settlement set forth in the Stipulation in all respects, and finds that said Settlement  
6 is, in all respects, fair, just, reasonable, and adequate to, and in the best interests of, Kratos,  
7 Kratos Stockholders, and Plaintiffs.

8           4.       This Court further finds the Settlement set forth in the Stipulation is the result of  
9 arm's-length negotiations between experienced counsel representing the interests of the Settling  
10 Parties. Accordingly, the Settlement embodied in the Stipulation is hereby approved in all  
11 respects and shall be consummated in accordance with its terms and provisions. The Settling  
12 Parties are hereby directed to perform the terms of the Stipulation.

13           5.       The Federal Action and all claims contained therein against the Settling  
14 Defendants are dismissed with prejudice. The Settling Parties are to bear their own costs, except  
15 as otherwise provided in the Stipulation.

16           6.       The publication of the Summary Notice of Pendency and Settlement of Derivative  
17 Actions (the "Summary Notice") and posting and filing of the Notice of Pendency and Settlement  
18 of Derivative Actions (the "Notice") on the websites of Kratos and Robbins Umeda LLP, and via  
19 a Form 8-K with the SEC, respectively, as provided for in the Order Granting Settling Parties'  
20 Joint Motion for Preliminary Approval of Settlement and Providing Notice constituted the best  
21 notice practicable under the circumstances to Current Kratos Stockholders and met the  
22 requirements of California and/or Delaware law, due process under the United States  
23 Constitution, and any other applicable law and constituted due and sufficient notice to all Persons  
24 entitled thereto.

---

25           <sup>1</sup> In March 2007 and February 2008, the Court determined that it lacked personal  
26 jurisdiction over Specially Appearing Defendants Gregory Jacobsen, Farzad Ghassemi, William  
27 Hogle, Scott I. Anderson, and Scot Jarvis. In accordance with the Parties' Stipulation,  
28 Specially Appearing Defendants agreed to waive personal jurisdiction for the limited purpose to  
effectuate the Settlement and Judgment.

1           7.       Upon the Effective Date, Plaintiffs, on behalf of themselves and, to the fullest  
2 extent permitted by law, on behalf of Kratos Stockholders shall be deemed to have, and by  
3 operation of this Judgment shall have, fully, finally, and forever released, relinquished, and  
4 discharged all Released Claims (including Unknown Claims), and any and all claims relating to  
5 or arising out of or connected with the Settlement or resolution of the Derivative Actions, against  
6 Individual Defendant Releasees and Kratos Releasees, except for obligations imposed by the  
7 Stipulation in connection with the Settlement.

8           8.       Upon the Effective Date, Kratos and Individual Defendants shall be deemed to  
9 have, and by operation of this Judgment shall have, fully, finally, and forever released,  
10 relinquished, and discharged Plaintiff Releasees from all claims (including Unknown Claims),  
11 arising out of, based upon or related to the institution, prosecution, assertion, settlement, or  
12 resolution of the Derivative Actions and/or the Released Claims, except for obligations imposed  
13 by the Stipulation in connection with the Settlement.

14           9.       Upon the Effective Date, each of the Individual Defendants shall be deemed to  
15 have, and by operation of this Judgment shall have, fully, finally, and forever released,  
16 relinquished, and discharged Kratos Releasees from all claims (including all Unknown Claims)  
17 arising out of, based upon or related to the institution, prosecution, assertion, settlement, or  
18 resolution of the Derivative Actions, except that the Individual Defendants, by virtue of this  
19 Judgment, have not released, relinquished, or discharged Kratos Releasees from any rights,  
20 claims, or causes of action for indemnification, including, but not limited to, insurance  
21 indemnification, and/or advancement of attorneys' fees and expenses (or other defense costs), for  
22 any matter whatsoever, required or permitted to the fullest extent under Kratos' Certificate of  
23 Incorporation or Bylaws, California or Delaware law, or any indemnification or similar  
24 agreement between Kratos and any such Individual Defendants.

25           10.      Upon the Effective Date, Kratos shall be deemed to have, and by operation of this  
26 Judgment shall have, fully, finally, and forever released, relinquished, and discharged all  
27 Released Claims (including Unknown Claims), and any and all claims relating to or arising out of  
28 or connected with the Settlement or resolution of the Derivative Actions, against Individual

1 Defendant Releasees, and Current Kratos Stockholders to the fullest extent permitted by law on  
2 behalf of themselves and each of their Related Parties are hereby forever barred and enjoined  
3 from commencing, instituting, or prosecuting derivatively any of the Released Claims, or any  
4 action or other proceeding brought derivatively on behalf of Kratos against any of the Released  
5 Claims (including Unknown Claims) against any of the Released Persons.

6 11. Upon the Effective Date, each of Individual Defendants shall be deemed to have,  
7 and by operation of this Judgment shall have, fully, finally, and forever released, relinquished,  
8 and discharged all Released Claims (including Unknown Claims), and any and all claims relating  
9 to or arising out of or connected with the Settlement or resolution of the Derivative Actions  
10 against the other Individual Defendant Releasees, except that Individual Defendants by virtue of  
11 this Stipulation have not released, relinquished, or discharged Kratos Releasees from any rights,  
12 claims, or causes of action for indemnification, including, but not limited to, insurance  
13 indemnification, and/or advancement of attorneys' fees and expenses (or other defense costs), for  
14 any matter whatsoever required or permitted to the fullest extent under Kratos' Certificate of  
15 Incorporation or Bylaws, California or Delaware law, or any indemnification or similar  
16 agreement between Kratos Releasees and any such Individual Defendants.

17 12. Neither the Stipulation nor the Settlement contained therein, nor any act performed  
18 or document executed pursuant to or in furtherance of the Stipulation or the Settlement: (a) is or  
19 may be deemed to be or may be used as an admission of, or evidence of, the validity of any  
20 claims released therein or by virtue of the releases attached thereto, including any of the Released  
21 Claims, or (b) may be deemed to be or may be used as an admission or evidence of any fault,  
22 wrongdoing, omission, or liability of any of the Settling Defendants, in any civil, criminal, or  
23 administrative proceeding in any court, administrative agency or other tribunal. Settling  
24 Defendants may file the Stipulation, the Judgment, and/or any document executed pursuant to or  
25 in furtherance of the Stipulation, in any action that may be brought against them in order to  
26 support a defense or counterclaim based on principles of *res judicata*, collateral estoppel, full  
27 faith and credit, release, judgment bar reduction, or any theory of claim preclusion or issue  
28 preclusion or similar defense or counterclaim.

1           13.     The Court hereby approves the Fees and Expenses Payment in accordance with the  
2 Stipulation and finds that the Fees and Expenses Payment is fair and reasonable.

3           14.     Without affecting the finality of this Judgment in any way, this Court hereby  
4 retains continuing jurisdiction over: (a) implementation of this Settlement; (b) the Settling Parties  
5 thereto for the purpose of construing, enforcing, and administering the Stipulation; and (c) any  
6 other matter related or ancillary thereto.

7           15.     The Court finds that the Derivative Actions were filed, prosecuted, and defended  
8 in good faith, and that during the course of the Derivative Actions, the Settling Parties and their  
9 respective counsel at all times complied with the requirements of Federal Rule of Civil  
10 Procedure 11, and all other similar rules and statutes.

11           16.     In the event that the Settlement does not become effective in accordance with the  
12 terms of the Stipulation or the Effective Date does not occur, then this Judgment shall be rendered  
13 null and void to the extent provided by and in accordance with the Stipulation and shall be  
14 vacated and, in such event, all orders entered and releases delivered in connection herewith shall  
15 be null and void to the extent provided by and in accordance with the Stipulation, and the Settling  
16 Parties shall be restored to their respective positions in the Derivative Actions as of January 5,  
17 2010.

18           17.     This Judgment is a final, appealable judgment and should be entered forthwith by  
19 the Clerk in accordance with Rule 58 of the Federal Rules of Civil Procedure.

20           **IT IS SO ORDERED.**

21 Dated: \_\_\_\_\_

By: \_\_\_\_\_  
HONORABLE JOHN A. HOUSTON  
UNITED STATES DISTRICT JUDGE

23 Submitted by:

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10 FACILITIES, INC.; Individual Defendants  
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12 ERIC DEMARCO, DAVID A. GARRISON,  
13 FRANKIE FARJOD, DAVID LEE, WILLIAM  
14 A. OWENS, BANDEL CARANO, JAMES R.  
15 EDWARDS, SCOTT FOX, DEANNA H.  
16 LUND, ANDREW M. LEITCH, LAURA  
17 SIEGAL, NAOMI D. WHITACRE, GEORGE  
18 WOZENCRAFT, and WILLIAM MAZILLY;  
19 and Specially Appearing Defendants FARZAD  
20 GHASSEMI, GREGORY JACOBSEN, SCOTT  
21 I. ANDERSON, SCOT JARVIS, and WILLIAM  
22 HOGLUND

23 ROBBINS UMEDA LLP  
24 BRIAN J. ROBBINS  
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Co-Lead Counsel for Plaintiffs

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UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF CALIFORNIA

IN RE WIRELESS FACILITIES, INC.,  
DERIVATIVE LITIGATION

Case No. 04-CV-1663 JAH (NLS)

**[PROPOSED] ORDER GRANTING  
SETTLING PARTIES' JOINT  
MOTION FOR PRELIMINARY  
APPROVAL OF SETTLEMENT  
AND PROVIDING NOTICE**

\_\_\_\_\_  
This Document Relates to:  
ALL ACTIONS.

**EXHIBIT B**

WHEREAS, the Settling Parties have jointly moved, pursuant to Federal Rule of Civil Procedure 23.1, for an order approving the settlement (the "Settlement") of the above-entitled action and the stockholder derivative action styled *In re Wireless Facilities, Inc. Derivative Litigation*, GIC 834253, currently pending in the Superior Court of the State of California, County of San Diego, in accordance with the Stipulation and Agreement of Settlement of Derivative Claims dated as of January 5, 2010 (the "Stipulation"), which, together with the Exhibits annexed thereto, sets forth the terms and conditions for the proposed Settlement of the litigation and for dismissal of the litigation with prejudice upon the terms and conditions set forth therein;

WHEREAS, for purposes of this preliminary approval order (the "Order"), all capitalized terms contained herein shall have the same meanings as set forth in the Stipulation (in addition to those capitalized terms defined herein); and

1 WHEREAS, the Court having read and considered the Stipulation and the Exhibits  
2 annexed thereto:

3 **NOW THEREFORE, IT IS HEREBY ORDERED:**

4 1. The Court preliminarily approves the Settlement of the litigation set forth in the  
5 Stipulation, as modified by this Order where applicable, subject to the right of any Current Kratos  
6 Stockholder to challenge the fairness, reasonableness, and adequacy of the Stipulation, and show  
7 cause, if any exists, why a final judgment dismissing the litigation based on the Stipulation should  
8 not be ordered herein after due and adequate notice to Current Kratos Stockholders has been  
9 given in conformity with this Order.

10 2. A hearing (the "Settlement Hearing") shall be held before this Court on  
11 \_\_\_\_\_, 20\_\_ at \_\_:\_\_ a./p.m. or as soon thereafter as counsel may be heard in the  
12 courtroom of the Honorable John A. Houston of the United States District Court for the Southern  
13 District of California, 940 Front Street, San Diego, CA 92101 to determine: (i) whether the  
14 proposed Settlement of the litigation as set forth in the Stipulation, should be approved in all  
15 respects as fair, just, reasonable, and adequate to, and in the best interests of, Kratos, Kratos  
16 Stockholders, and Plaintiffs; (ii) whether the Final Judgment and Order of Dismissal approving  
17 the Settlement should be entered; and (iii) whether the agreed-to Fees and Expenses Payment  
18 should be awarded to Plaintiffs' Counsel. The Court may adjourn or continue the Settlement  
19 Hearing without further notice to Current Kratos Stockholders.

20 3. The Court approves, as to form and content, the Summary Notice of Pendency and  
21 Settlement of Derivative Actions (the "Summary Notice"), substantially in the form of Exhibit B-  
22 1 attached hereto, for publication in a national financial newspaper, such as *Investor's Business*  
23 *Daily*, and a nationally recognized newswire, such as PR Newswire.

24 4. Not later than fifteen calendar days following notice of entry of this Order, Kratos  
25 shall cause the Summary Notice to be published in a national financial newspaper, such as  
26 *Investor's Business Daily*, and a nationally recognized newswire, such as PR Newswire.

27 5. The Court approves, as to form and content, the Notice of Pendency and  
28 Settlement of Derivative Actions (the "Notice"), substantially in the form of Exhibit B-2 as

1 attached hereto, for filing with the U. S. Securities and Exchange Commission (“SEC”) via a  
2 Form 8-K and for posting on the websites of Kratos and Robbins Umeda LLP.

3 6. Not later than fifteen calendar days following notice of entry of this Order, Kratos  
4 shall cause a copy of the Notice to be filed with the SEC via a Form 8-K and a copy of the Notice  
5 to be posted on its website.

6 7. Not later than fifteen calendar days following notice of entry of this Order,  
7 Robbins Umeda LLP shall cause a copy of the Notice to be posted on its website.

8 8. Kratos shall be solely responsible for, and shall cause to be paid, any costs  
9 associated with the publication, filing, and posting of the Summary Notice and the Notice.

10 9. The Court finds that dissemination of the Summary Notice and the Notice in the  
11 manner required by the Stipulation constitutes the best notice practicable under the circumstances  
12 to Current Kratos Stockholders and meets the requirements of California and/or Delaware law,  
13 due process under the United States Constitution, and any other applicable law and shall  
14 constitute due and sufficient notice to all Persons entitled thereto.

15 10. Kratos shall file with the Court and serve upon all parties no later than fourteen  
16 calendar days prior to the Settlement Hearing an affidavit or declaration describing the efforts  
17 taken to comply with this Order and stating that the publication of the Summary Notice and  
18 posting and filing of the Notice have been completed in accordance with the terms of this Order.

19 11. Plaintiffs' Counsel shall file with the Court and serve upon all parties no later than  
20 fourteen calendar days prior to the Settlement Hearing an affidavit or declaration stating that the  
21 posting of the Notice has been completed in accordance with the terms of this Order.

22 12. Any Current Kratos Stockholder who objects to the Settlement of the litigation  
23 shall have a right to appear and be heard at the Settlement Hearing. Any Current Kratos  
24 Stockholder may enter an appearance through counsel of their own choosing and at their own  
25 expense or may appear on their own. However, no Current Kratos Stockholder shall be heard at  
26 the Settlement Hearing unless, at least fourteen calendar days prior to the Settlement Hearing,  
27 such Person has: (1) filed with the Clerk of the Court a written objection to the Settlement setting  
28 forth: (a) the nature of the objection; (b) proof of ownership of Kratos capital stock through the

1 date of the Settlement Hearing, including the number of shares of Kratos capital stock and the  
2 date of purchase; and (c) any documentation in support of such objection; and (2) if a Current  
3 Kratos Stockholder intends to appear and requests to be heard at the Settlement Hearing, such  
4 stockholder must have, in addition to the requirements of (1) above, filed with the Clerk of the  
5 Court: (a) a written notice of such stockholder's intention to appear; (b) a statement that  
6 indicates the basis for such appearance; and (c) the identities of any witnesses the stockholder  
7 intends to call at the Settlement Hearing and the subjects of their testimony. If a Current Kratos  
8 Stockholder files a written objection and/or written notice of intent to appear, such stockholder  
9 must also simultaneously serve copies of such notice, proof, statement, and documentation,  
10 together with copies of any other papers or briefs such stockholder files with the Court (either by  
11 hand delivery or by first class mail) upon each of the following thereof:

12 ROBBINS UMEDA LLP  
13 BRIAN J. ROBBINS  
14 KEVIN A. SEELY  
15 REBECCA A. PETERSON  
16 DAVID L. MARTIN  
17 600 B Street, Suite 1900  
18 San Diego, CA 92101

16 FARUQI & FARUQI, LLP  
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19 Co-Lead Counsel for Plaintiffs

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24 San Diego, California 92130

23 Attorneys for Nominal Defendant WIRELESS FACILITIES, INC.; Individual Defendants  
24 THOMAS A. MUNRO, DANIEL STOKELY, ERIC DEMARCO, DAVID A. GARRISON,  
25 FRANKIE FARJOOD, DAVID LEE, WILLIAM A. OWENS, BANDEL CARANO, JAMES  
26 R. EDWARDS, SCOTT FOX, DEANNA H. LUND, ANDREW M. LEITCH, LAURA  
27 SIEGAL, NAOMI D. WHITACRE, GEORGE WOZENCRAFT, and WILLIAM MAZILLY;  
28 and Specially Appearing Defendants FARZAD GHASSEMI, GREGORY JACOBSEN, SCOTT  
I. ANDERSON, SCOT JARVIS, and WILLIAM HOGLUND

27 The written objections and copies of any papers and briefs in support thereof to be filed in  
28 Court shall be delivered by hand or sent by first class mail to:

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CLERK  
UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF CALIFORNIA  
940 Front Street,  
San Diego, CA 92101

Any Current Kratos Stockholder who does not make his, her, or its objection in the manner provided herein shall be deemed to have waived such objection and shall forever be foreclosed from making any objection to the fairness, reasonableness, or adequacy of the proposed Settlement, and shall otherwise be bound by the Judgment to be entered and the releases to be given.

13. The manner in which a notice of objection must be prepared, filed, and delivered shall be stated in the Summary Notice and Notice. Only Current Kratos Stockholders who have filed and delivered valid and timely written notices of objection will be entitled to be heard at the Settlement Hearing unless the Court orders otherwise.

14. All Kratos Stockholders shall be bound by all orders, determinations, and judgments in the Derivative Actions concerning the Settlement, whether favorable or unfavorable to Kratos Stockholders.

15. No later than seven calendar days before the Settlement Hearing, all briefs supporting the Settlement, including the Fees and Expenses Payment and any responses to stockholder objections, if any, shall be served and filed.

16. Neither the Stipulation, nor any of its terms or provisions, nor any of the negotiations or proceedings connected with it, shall be construed as an admission or concession by Settling Defendants of the truth of any of the allegations in the Derivative Actions, or of any liability, fault, or wrongdoing of any kind, or by Plaintiffs or any Kratos Stockholder of the merit of any defense or lack of merit of any claim.

17. Pending final determination of whether the Settlement should be approved, neither Plaintiffs, Kratos, nor any Kratos Stockholders shall commence, maintain, or prosecute against any of Settling Defendants, whether directly or derivatively on behalf of Kratos, any action or proceeding in any court or tribunal asserting any of the Released Claims, and all proceedings and

1 further activity between the Settling Parties in the Derivative Actions, except for those activities  
2 and proceedings relating to the Stipulation and the Settlement, shall be stayed.

3 18. The Court may, for good cause, extend any of the deadlines set forth in this Order  
4 without further notice to Current Kratos Stockholders and may approve the Settlement, with such  
5 modifications as may be agreed to by the Settling Parties, if appropriate, without further notice to  
6 Current Kratos Stockholders.

7 **IT IS SO ORDERED.**

8 Dated: \_\_\_\_\_

By: \_\_\_\_\_  
HONORABLE JOHN A. HOUSTON  
UNITED STATES DISTRICT JUDGE

10 Submitted by:

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26 A. OWENS, BANDEL CARANO, JAMES R.  
27 EDWARDS, SCOTT FOX, DEANNA H.  
28 LUND, ANDREW M. LEITCH, LAURA  
SIEGAL, NAOMI D. WHITACRE, GEORGE  
WOZENCRAFT, and WILLIAM MAZILLY;  
and Specially Appearing Defendants FARZAD  
GHASSEMI, GREGORY JACOBSEN, SCOTT  
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13 Co-Lead Counsel for Plaintiffs

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UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF CALIFORNIA

IN RE WIRELESS FACILITIES, INC.,  
DERIVATIVE LITIGATION

Case No. 04-CV-1663 JAH (NLS)

**SUMMARY NOTICE OF  
PENDENCY AND SETTLEMENT  
OF DERIVATIVE ACTIONS**

This Document Relates to:

**EXHIBIT B-1**

ALL ACTIONS.

**TO: ALL HOLDERS OF KRATOS DEFENSE & SECURITY SOLUTIONS, INC. (F/K/A WIRELESS FACILITIES, INC.) (“KRATOS”) CAPITAL STOCK AS OF JANUARY 5, 2010 (“CURRENT KRATOS STOCKHOLDERS”).**

**YOU ARE HEREBY NOTIFIED**, that the parties to the above derivative action and the stockholder derivative action styled *In re Wireless Facilities, Inc. Derivative Litigation*, GIC 834253, currently pending in the Superior Court of the State of California, County of San Diego (the “Derivative Actions”) have entered into a Stipulation and Agreement of Settlement of Derivative Claims (the “Stipulation”) to resolve the issues raised by the Derivative Actions (the “Settlement”).

PLEASE BE FURTHER ADVISED that pursuant to an Order of the United States District Court for the Southern District of California (the “Court”), a hearing (the “Settlement Hearing”) shall be held before this Court on \_\_\_\_\_, 20\_\_ at \_\_:\_\_ a./p.m. or as soon thereafter as counsel may be heard in the courtroom of the Honorable John A. Houston of the United States District Court for the Southern District of California, 940 Front Street, San Diego,

1 CA 92101 to determine: (i) whether the proposed Settlement of the litigation as set forth in the  
2 Stipulation, should be approved in all respects as fair, just, reasonable, and adequate to, and in the  
3 best interests of, Kratos, Kratos Stockholders, and Plaintiffs; (ii) whether the Final Judgment and  
4 Order of Dismissal approving the Settlement should be entered; and (iii) whether the agreed-to  
5 Fees and Expenses Payment should be awarded to Plaintiffs' Counsel. The Court may adjourn or  
6 continue the Settlement Hearing without further notice to Current Kratos Stockholders.

7 If you are a Kratos Stockholder, your rights to pursue certain derivative claims on behalf  
8 of Kratos may be affected by this Settlement.

9 A detailed Notice of Pendency and Settlement of Derivative Actions describing the  
10 Derivative Actions, the proposed Settlement, and the rights of Kratos Stockholders with regard to  
11 the Settlement was published as a Company Current Report on Form 8-K on \_\_\_\_\_, 2010,  
12 and was filed with the United States Securities and Exchange Commission (the "SEC") on that  
13 date. If you are a Kratos Stockholder and wish to receive a copy of the detailed Notice, you may  
14 obtain a copy by referring to the SEC's website at [www.sec.gov](http://www.sec.gov). You may also find information  
15 concerning the Settlement, including a copy of the Stipulation and the Notice, at the website of  
16 Robbins Umeda LLP at [www.robbinsumeda.com](http://www.robbinsumeda.com) and at the Company's website at  
17 [www.kratosdefense.com](http://www.kratosdefense.com).

18 A Current Kratos Stockholder wishing to assert an objection to the Settlement should, no  
19 later than \_\_\_\_\_, 2010:

20 (i) file with the Clerk of the Court a written objection to the Settlement setting  
21 forth: (a) the nature of the objection; (b) proof of ownership of Kratos capital stock through the  
22 date of the Settlement Hearing, including the number of shares of Kratos capital stock and the  
23 date of purchase; and (c) any documentation in support of such objection; and

24 (ii) if a Current Kratos Stockholder intends to appear and requests to be heard  
25 at the Settlement Hearing, such stockholder must, in addition to the requirements of subsection (i)  
26 above, file with the Clerk of the Court: (a) written notice of such stockholder's intention to  
27 appear; (b) a statement that indicates the basis for such appearance; and (c) the identities of any  
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1 witnesses the stockholder intends to call at the Settlement Hearing and the subjects of their  
2 testimony; and

3 (iii) if a Current Kratos Stockholder files a written objection and/or written  
4 notice of intent to appear, such stockholder must also simultaneously serve copies of such notice,  
5 proof, statement and documentation, together with copies of any other papers or briefs such  
6 stockholder files with the Court (either by hand delivery or by first class mail) upon each of the  
7 following:

8 CLERK  
9 UNITED STATES DISTRICT COURT  
10 SOUTHERN DISTRICT OF CALIFORNIA  
11 940 Front Street,  
12 San Diego, CA 92101  
13 ROBBINS UMEDA LLP

14 BRIAN J. ROBBINS  
15 KEVIN A. SEELY  
16 REBECCA A. PETERSON  
17 DAVID L. MARTIN  
18 600 B Street, Suite 1900  
19 San Diego, CA 92101

20 FARUQI & FARUQI, LLP  
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24 New York, NY 10017

25 Co-Lead Counsel for Plaintiffs

26 MORRISON & FOERSTER LLP  
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OWENS, BANDEL CARANO, JAMES R. EDWARDS, SCOTT FOX, DEANNA H.  
LUND, ANDREW M. LEITCH, LAURA SIEGAL, NAOMI D. WHITACRE,  
GEORGE WOZENCRAFT, and WILLIAM MAZILLY; and Specially Appearing  
Defendants FARZAD GHASSEMI, GREGORY JACOBSEN, SCOTT I.  
ANDERSON, SCOT JARVIS, and WILLIAM HOGLUND

Any Current Kratos Stockholder who does not timely make his, her, or its objection to the  
Settlement shall be deemed to have waived such objection and shall forever be foreclosed from

1 making any objection to the fairness, reasonableness, or adequacy of the proposed Settlement,  
2 and shall otherwise be bound by the judgments to be entered on the releases given.

3 **PLEASE DO NOT TELEPHONE THE COURT OR KRATOS**  
4 **REGARDING THIS NOTICE**

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UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF CALIFORNIA

IN RE WIRELESS FACILITIES, INC.,  
DERIVATIVE LITIGATION

Case No. 04-CV-1663 JAH (NLS)

**NOTICE OF PENDENCY AND  
SETTLEMENT OF DERIVATIVE  
ACTIONS**

\_\_\_\_\_  
This Document Relates to:

**EXHIBIT B-2**

ALL ACTIONS.

**TO: ALL HOLDERS OF KRATOS DEFENSE & SECURITY SOLUTIONS, INC. (FORMERLY KNOWN AS WIRELESS FACILITIES, INC.) (“KRATOS” OR THE “COMPANY”) CAPITAL STOCK AS OF JANUARY 5, 2010 (“CURRENT KRATOS STOCKHOLDERS”). PLEASE READ THIS NOTICE CAREFULLY. IT MAY AFFECT YOUR RIGHTS.**

**THIS NOTICE RELATES TO A PROPOSED SETTLEMENT OF STOCKHOLDER DERIVATIVE ACTIONS AND RELATED CLAIMS. CURRENT KRATOS STOCKHOLDERS ARE ENTITLED TO OBJECT, IF THEY DESIRE, TO THE SETTLEMENT AS DESCRIBED HEREIN.**

**IF THE COURT APPROVES THE SETTLEMENT, YOU WILL BE BARRED FROM CONTESTING THE FAIRNESS, REASONABLENESS, OR ADEQUACY OF THE PROPOSED SETTLEMENT, AND FROM PURSUING THE SETTLED CLAIMS.**

**YOU ARE HEREBY NOTIFIED**, pursuant to Federal Rule of Civil Procedure 23.1 and an Order of the United States District Court for the Southern District of California (the “Court”), that a proposed settlement (the “Settlement”) has been reached among Plaintiffs,<sup>1</sup> on behalf of

<sup>1</sup> For purposes of this Notice, the Court incorporates by reference the definitions in the Parties’ Stipulation and Agreement of Settlement of Derivative Claims (“Stipulation”), and all

(Footnote continues on next page.)  
CASE NO. 04-CV-1663 JAH (NLS)

1 nominal defendant Kratos, Individual Defendants, and Kratos in connection with *In re Wireless*  
2 *Facilities, Inc. Derivative Litigation*, Master File No. 04-CV-1663 JAH (NLS) (the “Federal  
3 Action”), currently pending in this Court, and *In re Wireless Facilities, Inc. Derivative Litigation*,  
4 GIC 834253 (the “State Action”), currently pending in the Superior Court of the State of  
5 California, County of San Diego (collectively, the “Derivative Actions”).<sup>2</sup>

6 The Derivative Actions have been brought derivatively on behalf of Kratos to remedy the  
7 harm allegedly caused to the Company by the defendants’ alleged violations of Federal and State  
8 law and breaches of fiduciary duties. The proposed Settlement, if approved by the Court, would  
9 fully, finally, and forever resolve the Derivative Actions on the terms and conditions summarized  
10 in this Notice.

11 A hearing (the “Settlement Hearing”) shall be held before this Court on  
12 \_\_\_\_\_, 20\_\_ at \_\_:\_\_ a/p.m. or as soon thereafter as counsel may be heard in the  
13 courtroom of the Honorable John A. Houston of the United States District Court for the Southern  
14 District of California, 940 Front Street, San Diego, CA 92101 to determine: (i) whether the  
15 proposed Settlement of the litigation as set forth in the Stipulation, should be approved in all  
16 respects as fair, just, reasonable, and adequate to, and in the best interests of, Kratos, Kratos  
17 Stockholders, and Plaintiffs; (ii) whether the Final Judgment and Order of Dismissal approving  
18 the Settlement should be entered; and (iii) whether the agreed-to Fees and Expenses Payment  
19 should be awarded to Plaintiffs’ Counsel.

20 This Notice is not intended to be and should not be construed as an expression of any  
21 opinion by the Court with respect to the truth of the allegations of the claims in the Derivative  
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23 \_\_\_\_\_  
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24 capitalized terms used herein shall have the same meanings as set forth in the Stipulation. A copy  
25 of the Stipulation may be found at the websites of Robbins Umeda LLP at  
www.robbinsumeda.com and the Company's website at www.kratosdefense.com.

26 <sup>2</sup> In September 2008, this Court preliminarily approved settlement of the 2004 Federal Class  
27 Action. In January 2009, the Court granted final approval of the proposed settlement terms,  
issued its final judgment on the matter, and entered an order dismissing the case with prejudice.

1 Actions or the merits of the claims or defenses asserted. This Notice is merely to advise you of  
2 the pendency and proposed Settlement and of your rights thereunder.

3 **I. SUMMARY OF THE DERIVATIVE ACTIONS**

4 In August 2004, Kratos announced, following an extensive analysis of its contingent tax  
5 liabilities, its intention to restate its financial statements for fiscal years ended 2000 through 2003  
6 to accrue for certain foreign tax contingencies. The day after the Company's August 2004  
7 announcement, and roughly a month before it released the full details of the restatement, the first  
8 of fourteen lawsuits — ten federal securities class actions, two federal derivative actions, and two  
9 state derivative actions — was filed. The ten securities class actions were subsequently  
10 consolidated into a single action before this Court — *In re Wireless Facilities, Inc. Securities*  
11 *Litigation*, Master File No. 04-CV-1589 JAH (NLS) (S.D. Cal) (the “2004 Federal Class  
12 Action”). Similarly, in 2005 the two federal derivative lawsuits, brought separately by Michael  
13 Roth and Rosario Pedicini (“Federal Plaintiffs”), were consolidated into the Federal Action. The  
14 two state derivative lawsuits, brought separately by Mary Beth Joseph and Robert Casden (“State  
15 Plaintiffs”), were consolidated into the State Action (State Plaintiffs and Federal Plaintiffs are  
16 collectively referred to herein as “Plaintiffs”).<sup>3</sup>

17 In March 2005, Federal Plaintiffs filed their Consolidated Verified Shareholder Derivative  
18 Complaint for violations of California Corporations Code, Breach of Fiduciary Duty, Abuse of  
19 Control, Gross Mismanagement, Waste of Corporate Assets, Unjust Enrichment and Violation of  
20 the Sarbanes-Oxley Act of 2002 (“Consolidated Complaint”) against sixteen current or former  
21 officers, directors, and employees of Kratos. Federal Plaintiffs alleged that these individuals  
22 failed to properly account for foreign tax contingencies, failed to exercise appropriate oversight,  
23 engaged in unlawful insider trading, and breached their fiduciary duties to the Company. Six of  
24 the individual defendants named in the Consolidated Complaint asserted they do not live in  
25 California and moved to dismiss the Consolidated Complaint on the ground that the Court lacked

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27 <sup>3</sup> Prior to any response by the defendants to the State Action, the matter was stayed (and  
28 remains so) by the San Diego Superior Court pending resolution of the Federal Action.

1 personal jurisdiction over them. The Court did not require any response from the remaining  
2 individual defendants who were not contesting the Court's jurisdiction until after the Court had  
3 decided the jurisdictional issue. In March 2007, following jurisdictional discovery, the Court  
4 granted the motion to dismiss for lack of personal jurisdiction as to five of the six contesting  
5 defendants and dismissed them from the case.

6 In March 2007, Kratos announced that it was conducting an internal investigation into its  
7 historical stock option grant practices going back to 1998. Kratos also announced that it had  
8 identified some option "grants issued between 1998 and 2003 that require[d] further review  
9 because their historical measurement dates appear[ed] incorrect and [were] expected to result in  
10 adjustments affecting previously issued financial statements." The announcement stated that it  
11 was likely that Kratos would restate its financial statements for fiscal years 2000 to 2005.

12 Two weeks after the Company's public announcement that it was conducting the internal  
13 stock option review, Federal Plaintiffs filed their Verified Consolidated Amended Shareholder  
14 Derivative Complaint for violations of California Corporations Code, Breach of Fiduciary Duty,  
15 Abuse of Control, Gross Mismanagement, Waste of Corporate Assets, Unjust Enrichment,  
16 Violation of the Sarbanes-Oxley Act of 2002, Accounting, Rescission and Constructive Trust  
17 ("Amended Complaint") against all of the individuals originally named in the prior Consolidated  
18 Complaint, including those previously dismissed for lack of jurisdiction. Federal Plaintiffs also  
19 added nine new defendants, including an additional defendant who asserted that he did not live in  
20 California.

21 The Amended Complaint contains the same financial reporting and accounting allegations  
22 arising from the 2004 restatement as the prior Consolidated Complaint. As for the amended  
23 allegations, Federal Plaintiffs added allegations that certain defendants "backdated" or  
24 "springloaded" employee stock option grants so that the options were granted at less than fair  
25 market value.<sup>4</sup>

26 <sup>4</sup> In April 2007, purported Kratos stockholder Eamen Hameed filed a federal derivative  
27 complaint purportedly on behalf of Kratos and against a subset of the same current and/or former  
28 officers and directors named in the Federal and State Actions — *Hameed v. Tayebi*, No. 07-CV-  
0680 BTM (RBB) (S.D. Cal.) (the "Hameed Action"). The Hameed Action arose from Kratos'

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1 In July 2007, the five defendants previously dismissed for lack of personal jurisdiction,  
2 joined now by an additional defendant who asserted lack of personal jurisdiction, moved to  
3 dismiss the Amended Complaint on the ground that the Court still lacked jurisdiction over them  
4 despite the new stock option allegations. Again, the remaining defendants were not required to  
5 respond to the Amended Complaint until the Court determined the jurisdictional issues.

6 In February 2008, the Court granted the jurisdictional motion to dismiss as to the  
7 previously-dismissed defendants and again dismissed them from the Federal Action, but denied  
8 the motion as to newly-added defendant (“February 2008 Order”). Federal Plaintiffs  
9 subsequently moved the Court for certification and entry of final judgment of the Court’s  
10 February 2008 Order so that Federal Plaintiffs might appeal the February 2008 Order to the Ninth  
11 Circuit Court of Appeals. In July 2008, the Court granted Federal Plaintiffs’ motion for  
12 certification. Federal Plaintiffs filed a notice of appeal of the February 2008 Order in August  
13 2008. Due to the concurrent settlement efforts described below, Federal Plaintiffs have not filed  
14 their opening appellate briefs and none of the defendants named in the Federal Action have  
15 responded to the Consolidated Complaint or Amended Complaint.

## 16 **II. THE SETTLEMENT EFFORTS**

17 In August 2008, in an effort to resolve the Derivative Actions, Kratos, Plaintiffs (on behalf  
18 of themselves and Kratos), and each of the Individual Defendants (the “Settling Parties”), along  
19 with Kratos’ directors and officers liability insurance carriers, mediated the matters before Judge

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21 March 2007 announcement that it was conducting the internal stock option review and alleged  
22 that certain defendants allowed company insiders to backdate stock option grants, so that stock  
23 options were priced below fair market value on the day they were actually granted, and that as a  
24 result, Kratos’ relevant U.S. Securities and Exchange Commission (“SEC”) filings were false and  
25 misleading. On August 18, 2008, Hameed voluntarily dismissed the Hameed Action pursuant to  
26 Federal Rule of Civil Procedure 41(a). Additionally, in November 2007, a consolidated federal  
27 class action securities lawsuit — *In re Wireless Facilities, Inc. Securities Litigation II*, Master  
28 File No. 07-CV-00482-BTM (NLS) (S.D. Cal.) (the “2007 Federal Class Action”) — was filed in  
this Court, alleging that Kratos backdated or springloaded employee stock option grants. On  
September 3, 2008, this Court preliminarily approved settlement of the 2007 Federal Class  
Action. On December 19, 2008, this Court granted final approval of the proposed settlement  
terms, issued its final judgment on the matter, and entered an order dismissing the case with  
prejudice.

1 Daniel Weinstein (Ret.) of JAMS, a highly skilled and experienced mediator. While a settlement  
2 agreement was not reached during the mediation, the Settling Parties and the insurers, along with  
3 the assistance of the mediator, continued to pursue extensive good-faith settlement negotiations.  
4 In addition, certain of the Settling Parties participated in further in-person meetings with the  
5 mediator in February 2009. While a settlement agreement was not reached following the  
6 February 2009 meetings, the Settling Parties, along with the assistance of the mediator, continued  
7 to pursue additional extensive good-faith settlement negotiations. In October 2009, the Settling  
8 Parties agreed in principle to settle the Derivative Actions on terms set forth in the Stipulation, as  
9 summarized below, and subject to Court approval.

### 10 **III. PLAINTIFFS' CLAIMS AND BENEFITS OF SETTLEMENT**

11 Plaintiffs believe that the claims asserted in the Derivative Actions have merit. However,  
12 Plaintiffs' Counsel recognize and acknowledge the expense and length of continued proceedings  
13 necessary to prosecute the Derivative Actions on behalf of Kratos through at least one appeal and  
14 potentially through trial. Plaintiffs' Counsel have conducted an investigation of the claims  
15 asserted in the Derivative Actions, including research of publicly available information and  
16 review of certain documents requested by and provided to Plaintiffs' Counsel by Kratos and  
17 certain defendants. Plaintiffs' Counsel also have taken into account the uncertain outcome and  
18 the risk of any litigation, especially in complex actions such as the Derivative Actions, as well as  
19 the difficulties and delays inherent in such litigation. Plaintiffs' Counsel also are mindful of the  
20 inherent problems of proof of, and possible defenses to, the causes of action asserted in the  
21 Derivative Actions. Plaintiffs' Counsel believe that the Settlement set forth in the Stipulation  
22 confers substantial benefits upon, and is in the best interest of, Kratos, its stockholders, and  
23 Plaintiffs.

### 24 **IV. SETTLING DEFENDANTS' DENIAL OF WRONGDOING AND LIABILITY**

25 Kratos and each of Individual Defendants (collectively, "Settling Defendants") have  
26 denied and continue to deny each and all of the claims and contentions alleged in the Derivative  
27 Actions. The Individual Defendants expressly have denied and continue to deny all charges of  
28 wrongdoing or liability against them or any of them arising out of any of the conduct, statements,

1 acts, or omissions alleged, or that could have been alleged, in the Derivative Actions. The  
2 Settling Defendants also have denied and continue to deny, *inter alia*: (i) that they violated the  
3 federal securities laws, violated state law, or breached their fiduciary duties; (ii) the allegations  
4 that Kratos has suffered damage; (iii) that the price of Kratos securities was artificially inflated by  
5 reason of alleged misrepresentations, non-disclosures, or otherwise; (iv) that Kratos was harmed  
6 by any of the conduct alleged in the Derivative Actions; and (v) that a majority of the Board of  
7 Kratos was not independent and disinterested during the relevant periods.

8 Nonetheless, the Settling Defendants have concluded that further conduct of the  
9 Derivative Actions would be protracted, expensive, and distracting to themselves, Kratos, and its  
10 management, and that it is desirable and beneficial to them that the Derivative Actions be fully  
11 and finally settled in the manner and upon the terms and conditions set forth in the Stipulation, in  
12 order to limit further expense, inconvenience, and distraction, and to dispose of the burden of  
13 protracted litigation. The Settling Defendants have also taken into account the uncertainty and  
14 risks inherent in any litigation, especially in complex cases like these Derivative Actions. Kratos  
15 has determined that it is in its best interest to enter into the Stipulation because Kratos will receive  
16 substantial benefits from the agreed-upon Settlement.

## 17 **V. THE PROPOSED SETTLEMENT**

18 Plaintiffs (on behalf of themselves and derivatively on behalf of Kratos), nominal  
19 defendant Kratos, and the Individual Defendants, by and through their respective counsel or  
20 attorneys of record, have stipulated and agreed that, subject to the approval of the Court, the  
21 Derivative Actions and the Released Claims, as defined below, shall be finally and fully  
22 compromised, settled, and released, and the Derivative Actions shall be dismissed with prejudice  
23 as to the Settling Parties, upon and subject to the terms and conditions of the Stipulation, as  
24 summarized below.

### 25 **A. Return of Stock Options**

26 In connection with the Settlement of the Derivative Actions, the individuals indentified  
27 immediately below agree to provide the following consideration to Kratos within thirty days from  
28 the date the Judgment become Final.

1           1.       Masood Tayebi and Massih Tayebi agree to forfeit, collectively, a total of 50,000  
2 shares of Kratos stock to Kratos.

3           2.       Scott I. Anderson agrees to forfeit a total of 2,000 shares of Kratos stock to Kratos.

4           3.       Scot Jarvis agrees to forfeit a total of 2,000 shares of Kratos stock to Kratos.

5           4.       Farhad Farjood agrees to forfeit to Kratos any and all claims relating to 10,000  
6 options to purchase shares of Kratos stock.

7           5.       To the extent that Brad Weller still owns or controls any options to purchase  
8 shares of Kratos stock, he agrees to forfeit to Kratos any and all claims relating to 10,000 options  
9 to purchase shares of Kratos stock, or all options to purchase shares of Kratos stock if Mr. Weller  
10 holds less than 10,000 options.

11          6.       To the extent that Thomas Munro still owns or controls any options to purchase  
12 shares of Kratos stock, he agrees to forfeit to Kratos any and all claims relating to 10,000 options  
13 to purchase shares of Kratos stock, or all options to purchase shares of Kratos stock if Mr. Munro  
14 holds less than 10,000 options.

15          7.       To the extent that Terry Ashwill still owns or controls any options to purchase  
16 shares of Kratos stock, he agrees to forfeit to Kratos any and all claims relating to 10,000 options  
17 to purchase shares of Kratos stock, or all options to purchase shares of Kratos stock if  
18 Mr. Ashwill holds less than 10,000 options.

19           **B.       Corporate Governance Measures**

20           In full and final settlement of the Derivative Actions, the Board of Directors (the “Board”)  
21 of Kratos has agreed to adopt, or to maintain where already implemented, the corporate  
22 governance measures outlined below within thirty days from the date the Judgment becomes  
23 Final and will keep such measures in force and effect for a period of no less than four years from  
24 the date the Judgment becomes Final, except as stated otherwise in section 10(b) below. Kratos  
25 acknowledges that Plaintiffs’ actions were a direct and material factor in the corporate  
26 governance policies that have been enacted since the filing of the Derivative Actions and were a  
27 material factor in the enactment of the measures that will be adopted within thirty days from the  
28 date the Judgment becomes Final.

1           1.     The Board of Directors

2                   (a)     The Board shall adopt a resolution that requires all directors, including the  
3 current Board, to attend annually at least one corporate governance class that is designed to keep  
4 corporate directors abreast of trends in governance and aware of their fiduciary, legal, and ethical  
5 responsibilities.

6                   (b)     The Board shall adopt the appropriate resolutions to implement the  
7 following corporate governance reforms:

8                           (i)     the Company’s Board shall be increased by two Independent  
9 Directors within eighteen months from the date the Judgment becomes Final;

10                           (ii)    each director of the Company shall be elected to the Board by  
11 majority vote;

12                           (iii)  no individual member of the Board shall be the Chairman of more  
13 than one Board committee;

14                           (iv)   each director of the Company shall be required to certify in writing  
15 annually that he or she has received, read, and understands the guidelines for directors set forth in  
16 the Company’s Code of Legal and Ethical Conduct;

17                           (v)    the performance of the Chairman of the Board shall be evaluated by  
18 the Board annually. Should the remaining directors determine that the Board Chairman is not  
19 sufficiently active or successful in providing meaningful leadership for the Board, he or she shall  
20 be replaced as the Chairman;

21                           (vi)   the Company’s independent registered public auditing firm may not  
22 perform any consulting work for the Company, other than tax consulting work;

23                           (vii)  the Company’s Chief Executive Officer (“CEO”) and Chief  
24 Financial Officer (“CFO”) shall be responsible for ensuring that the Company’s revenue  
25 recognition policy, which conforms to the requirements of GAAP as currently in effect or as  
26 amended, is implemented and utilized throughout the Company. The CEO and CFO shall report  
27 to the Board on an annual basis regarding the implementation and operation of this policy. The  
28 CEO and CFO shall distribute the Company’s revenue recognition policy to each such Company

1 employee who records or reviews the recording of revenue and ensure that each such Company  
2 employee completes an employee training program concerning the Company's policy on revenue  
3 recognition. Any questions regarding that policy or training program, or the application of the  
4 policy, shall be directed to the Company's CFO, who shall inform the CEO; and

5 (viii) at each regularly scheduled Board meeting, the Company's CFO (or  
6 his or her designee) shall provide a report as to the Company's financial condition and prospects,  
7 including, but not limited to, a discussion of any material decreases in revenues and earnings, if  
8 any, management plans for ameliorating or reversing such negative trends and the success or  
9 failure of any such plans presented in the past.

10 2. Responsibilities of the Independent Directors

11 (a) The Board shall adopt a resolution requiring that a majority of the members  
12 of the Board shall be Independent Directors, as defined fully in the Stipulation.

13 (b) The Independent Directors shall meet separately from the rest of the Board  
14 on a quarterly basis.

15 3. Board Committees

16 (a) The Board will re-institute its Nominating and Corporate Governance  
17 Committees consisting of no less than two Independent Directors to oversee the nomination of the  
18 additional director(s), and to implement and oversee appropriate corporate governance reforms.

19 (b) The Board's committees shall have standing authorization, in their own  
20 discretion, to retain legal or other advisors of their choice, who shall report directly to the Board  
21 or committee.

22 (c) The Bylaws of the Company shall be revised to include specific limits on  
23 outside board memberships. The CEO of the Company shall not participate on the board of  
24 directors of any more than one additional for-profit corporation (either publicly traded or  
25 privately held) for a period of two years,<sup>5</sup> and a majority of Independent Directors shall not serve

26 <sup>5</sup> The CEO will be permitted to serve on the board of directors of not more than one  
27 additional company with advance consent of the Nominating and Corporate Governance  
28 Committee. In general, however, the CEO shall devote his or her full energies to running the  
Company.

1 on more than three boards of directors of publicly held companies, including the Company. Any  
2 CEO or other full-time senior corporate officer of another company serving on the Company's  
3 Board shall be limited to not more than two public company boards of directors in total, including  
4 the boards of directors of such person's own employer and the Company.

5 4. Compensation Committee

6 (a) The Company shall have a Compensation Committee Charter that  
7 expressly vests in the Compensation Committee the responsibility and obligation to:

8 (i) approve the Company's stock option grants, including the approval  
9 of employees and parties who are to receive stock option grants and the details of those option  
10 grants; and

11 (ii) prevent the granting, issuance, or approval of any stock options that  
12 have been or can be market-timed, backdated, or otherwise manipulated.

13 (b) The Compensation Discussion and Analysis written for the Company's  
14 annual Proxy Statement shall address efforts undertaken by the Compensation Committee to  
15 design and implement systems and controls to prevent the granting, issuance, and/or approval of  
16 market-timed, backdated, or manipulated stock option grants.

17 (c) The Compensation Committee shall not delegate its authority to grant stock  
18 options to a Stock Option Administrator unless the delegated Stock Option Administrator is a  
19 member of the Compensation Committee of the Board. If a Stock Option Administrator is  
20 delegated the authority to grant stock options, any stock option grant by the Stock Option  
21 Administrator must be approved by the entire Compensation Committee.

22 (d) The Compensation Committee shall select and retain an independent  
23 compensation consultant to provide advice and guidance to the Committee as needed. In  
24 addition, the consultant shall, at such times as requested by the Committee, conduct a  
25 comparative market study of the Company's executive compensation policies, practices, and  
26 procedures. This study shall be delivered to the Compensation Committee for its use in  
27 evaluating and revising, if necessary, the compensation structure for the Company's executives.  
28

1           5.     Enhanced Internal Audit Function

2                   (a)     The Company shall implement and maintain an enhanced internal audit  
3 function. The Company's outside auditor shall not provide this service. The Internal Auditor,  
4 who shall be approved by the Board and report directly to the Audit Committee at least annually,  
5 shall review the Company's internal control environment. The Internal Auditor shall be  
6 responsible for devising an Internal Audit Plan for each fiscal year that will be presented to the  
7 Audit Committee.

8                   (b)     A written report shall be prepared for each internal audit performed  
9 describing the internal audit's findings, opinions, and recommendations, if any. These written  
10 reports shall be directed to the CEO, CFO, and the Audit Committee for review and, if necessary,  
11 remedial action.

12           6.     Audit Committee

13                   (a)     The Audit Committee shall use its best efforts to have at least two members  
14 with an accounting or financial management background. If an Audit Committee member  
15 possessing such accounting or financial background resigns, is terminated, or otherwise is  
16 removed from his or her directorship on the Audit Committee, the Board shall use its best efforts  
17 to replace such director within ninety days of his or her departure with another director that has an  
18 accounting or financial management background. These best efforts shall include the  
19 commencement of a search to locate an additional Board member with an accounting or financial  
20 management background.

21                   (b)     The Audit Committee shall have a charter which includes the following  
22 provisions:

23                           (i)     meetings to be held, among other times, prior to the commencement  
24 and prior to the completion of the annual audit;

25                           (ii)    each meeting shall include a meeting with appropriate Company  
26 management, followed by an executive session with no management present; and

27                           (iii)  each meeting shall have a written agenda.

28                   (c)     The Audit Committee's responsibilities shall include:

1 (i) meeting with the Company's independent registered public  
2 accounting firm concerning:

3 (1) the reliability of the Company's forward-looking statements  
4 contained in interviews with media agencies, investor conference calls, committee reports,  
5 quarterly and annual reports, proxy statements, and press releases disseminated by the Company;  
6 and

7 (2) the reliability of the Company's statements relating to  
8 internal financial control mechanisms contained in interviews with media agencies, investor  
9 conference calls, committee reports, quarterly and annual reports, proxy statements, and press  
10 releases disseminated by the Company.

11 (ii) meeting with management to ascertain the Company's primary  
12 business exposure risks; and

13 (iii) meeting with the Company's Internal Auditors at year-end  
14 regarding:

15 (1) the nature of the internal audit plan, including the  
16 effectiveness and continued use of the policies and procedures of the internal audit plan;

17 (2) the appropriate staffing levels for the internal audit function;

18 (3) whether the Company's financial reporting policies and  
19 practices are sufficiently transparent; and

20 (4) whether the Company's financial reporting policies and  
21 practices are unusually aggressive.

22 7. Stock Option Granting Policies and Procedures

23 (a) The following stock-option related controls, that already have been  
24 implemented by the Company, will be maintained for a period of no less than four years from the  
25 date of entry of the Judgment:

26 (i) segregating certain responsibilities related to option granting and  
27 the execution of stock option exercise transactions, including, but not limited to, the Director of  
28 Financial Reporting being required to approve exercises and the Assistant Controller/Director of

1 Financial Reporting being required to separately review all entries to the Company's Equity Edge  
2 database by the Stock Option Administrator;

3 (ii) documenting and assessing the design and operating effectiveness  
4 of key internal controls over the stock administration function;

5 (iii) establishing processes and procedures to increase communications  
6 between the stock administration, human resources, and accounting functions, including, but not  
7 limited to, requiring communications between human resources and accounting/finance related to  
8 any separation agreement that might result in a modification of terms;

9 (iv) adding independent reviews and reconciliations of stock option  
10 activity separate from the stock administration function;

11 (v) establishing a consistent, formalized procedure for stock option  
12 award procedures including limiting the authority to approve stock option grants;

13 (vi) upgrading the equity tracking software program and system  
14 controls that support the processes and continuing to maintain the most current version of the  
15 option tracking software;

16 (vii) requiring and arranging for training for those employees who utilize  
17 the Company's equity tracking software program, as well as all those involved in the stock option  
18 granting process, to enhance awareness and understanding of legal, tax, and accounting  
19 implications;

20 (viii) requiring that only an employee independent of the stock  
21 administration function be allowed to communicate stock option exercise instructions to the  
22 Company's transfer agent;

23 (ix) requiring quarterly reconciliation of exercises according to transfer  
24 agent records versus exercises according to the Equity Edge database to identify any  
25 discrepancies;

26 (x) requiring approval by the Company's Compensation Committee  
27 during meetings rather than by use of Unanimous Written Consents;

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1 (xi) requiring the development of an annual option granting plan and  
2 option granting matrix;

3 (xii) dissolving the Company's non-officer stock option committee; and

4 (xiii) the grant date of all stock options shall be the fifteenth trading day  
5 of the month after which they are approved.

6 (b) All stock option plans adopted by the Company shall clearly define the  
7 exercise price, grant date, and the fair market value of stock. The exercise price or value of any  
8 equity award shall be determined by fair market value of the Company's stock on the date of the  
9 grant. The fair market value of the Company's stock shall be the closing price (or closing bid, if  
10 no sales were reported) for a share of the Company's stock on such days as quoted by the  
11 exchange or over-the-counter market on which the stock is listed.

12 (c) Any and all stock option plans that permit market timing or backdating of  
13 stock options are void and shall be without force or effect.

14 (d) Any substitute stock option plan(s) adopted by the Company in the future  
15 must expressly prohibit market timing and backdating of stock options.

16 (e) Any stock option plans shall give the Compensation Committee the sole  
17 and exclusive power and duty to administer the Company's stock option plans.

18 (f) Any and all disclosure requirements concerning executive compensation  
19 and stock option grants, including the Sarbanes-Oxley Act of 2002 disclosure requirements, shall  
20 be followed by the Company.

21 (g) All requirements of the Internal Revenue Code as they relate to the  
22 granting, issuance, timing, pricing, and treatment of stock options shall be observed and followed  
23 by the Company.

24 (h) The substance of the following clauses shall be included in any current  
25 and/or subsequent equity incentive plan, whether subject to stockholder approval or not:

26 (i) The exercise price for each stock option grant shall be at least 100%  
27 of the fair market value on the date of the grant;

28

1 (ii) the Company shall give notice of the determination to each  
2 employee or consultant to whom a stock option is so granted as soon as reasonably practicable,  
3 but in no event shall such notice be given more than thirty days after the date of such grant; and

4 (iii) authority to grant stock option awards shall be limited to the full  
5 Board or the Compensation Committee, consisting of three or more independent directors, and  
6 shall not be delegated to any other person or body.

7 8. Insider Trading Policy

8 The Company shall adopt an Insider Trading Policy that provides as follows:

9 (a) The Insider Trading Policy shall specifically prohibit all Company  
10 directors, officers and employees from trading in Company securities while in possession of  
11 material, non-public information regarding the Company, including, but not limited to: (i)  
12 material, non-public information regarding actual or estimated results of operations and earnings;  
13 (ii) material, non-public proposals or agreements relating to mergers, acquisitions or divestitures;  
14 and (iii) material, non-public information regarding significant contracts, patents, or new product  
15 development.

16 (b) The Insider Trading Policy shall encourage all directors and Section 16  
17 officers who wish to trade in Company securities to adopt a valid trading plan pursuant to SEC  
18 Rule 10b5-1, 17 C.F.R. § 240.10b5-1.

19 (c) The Insider Trading Policy shall require all other Company employees who  
20 wish to trade in Company securities to do so only within prescribed trading windows, to be  
21 established by the Board. All Company employees who have not adopted a valid Rule 10b5-1  
22 trading plan shall be prohibited from trading in Company securities except during open trading  
23 windows.

24 9. Related-Party Transactions

25 (a) The Company shall maintain its policy entitled "Conflict of Interest and  
26 Related Party Transactions," which became effective on October 9, 2007.

27 (b) Any material changes to the Conflict of Interest and Related Party  
28 Transactions Policy may be made only with the approval of the Board.

1           10.    Additional Controls

2                   (a)    The following additional controls that already have been implemented by  
3 the Company will be maintained for a period of no less than four years from the date of the entry  
4 of Judgment:

5                           (i)    The Company shall continue to maintain its internal Contracts  
6 Administration Department, which has been established to ensure that complete contract files are  
7 maintained to support the project estimate-at-completion computation. This is accomplished  
8 using a database in which all relevant contract administration documents are maintained. As a  
9 part of the revised revenue recognition procedures, the database is accessed to update information  
10 needed in the period-end estimate-at-completion.

11                           (ii)   In conjunction with the Company's month-end and year-end  
12 closing procedures, the Company has implemented additional monitoring and review controls  
13 over its estimate-at-completion calculations, as well as its invoicing/customer billings procedures  
14 and its valuation of accounts receivable balances.

15                           (iii)   Shareholder Nominated Director Process. The Independent  
16 Directors shall consider and evaluate recommendations for director nominees proposed by a  
17 qualified stockholder. The stockholder must submit its director nominee recommendation to the  
18 Corporate Secretary in writing and provide the following information:

19                                   (1)    a statement by the stockholder that: (i) the stockholder is  
20 the holder of at least 1% of the Company's capital stock; (ii) the stock has been held for at least  
21 one year prior to the date of the submission; and (iii) the stockholder will continue to hold the  
22 shares through the date of the annual stockholder meeting;

23                                   (2)    the candidate's name, age, contact information, and current  
24 principal occupation or employment;

25                                   (3)    a description of the candidate's qualifications and business  
26 experience during, at a minimum, the last five years, including the candidate's principal  
27 occupation or employment, and the name and principal business of any corporation or other  
28 organization in which the candidate was employed;

1 (4) the candidate's resume; and

2 (5) three references.

3 (iv) to be evaluated in connection with the Company's established  
4 procedures for evaluating potential director nominees, the qualifying stockholder must provide  
5 the stockholder's director nominee recommendation to the Company at least 120 days prior to the  
6 anniversary of the date proxy statements were mailed to stockholders in connection with the prior  
7 year's annual stockholder meeting.

8 (b) The Chairman of the Board must not simultaneously hold the position of  
9 CEO. Given the importance of finding an appropriate Chairman of the Board, the Company will  
10 have four years from the date the Judgment becomes Final to begin complying with this  
11 provision. This provision shall remain in effect for a period of no less than four years from the  
12 date on which the provision is first implemented.

13 **C. Restriction of Voting Rights**

14 In connection with the Settlement of the Derivative Actions, Masood Tayebi and Massih  
15 Tayebi hereby agree that for a period of no less than three years from the date the Judgment  
16 becomes Final, they will not exercise any of the voting rights associated with any of the shares of  
17 Kratos stock that they personally own or that they control through any trust or other entity.  
18 Masood Tayebi and Massih Tayebi shall provide the Company with a signed certification each  
19 year stating that they did not exercise any of the voting rights associated with any of the shares  
20 they own or control and did not make any material recommendations to anyone exercising voting  
21 rights in Kratos stock with respect to the exercise of those rights.

22 **VI. DISMISSAL AND RELEASES**

23 The full terms of the dismissal and release of claims are set forth in the Stipulation. The  
24 following is only a summary.

25 Upon the Effective Date, the Individual Defendants, Kratos, and Plaintiffs, on behalf of  
26 themselves and, to the fullest extent permitted by law, on behalf of all Kratos Stockholders shall  
27 be deemed to have released the Released Claims against the other Individual Defendant  
28 Releasees, except for the obligations imposed by the Stipulation in connection with the

1 Settlement. Moreover, the Final Judgment and Order of Dismissal with Prejudice (“Judgment”),  
2 to be entered upon approval of the Settlement, will preclude the filing of any action purporting to  
3 litigate the Released Claims against the Individual Defendant Releasees and Kratos Releasees.  
4 Upon the Effective Date, Kratos and the Individual Defendants shall be deemed to have released  
5 Plaintiff Releasees from all claims arising out of, based upon or related to the institution,  
6 prosecution, assertion, settlement, or resolution of the Derivative Actions and/or the Released  
7 Claims, except for the obligations imposed by the Stipulation in connection with the Settlement.  
8 Also upon the Effective Date, each of the Individual Defendants and Plaintiffs, on behalf of  
9 themselves and, to the fullest extent permitted by law, on behalf of all Kratos Stockholders, shall  
10 be deemed to have released Kratos Releasees from all claims arising out of, based upon or related  
11 to the institution, prosecution, assertion, settlement, or resolution of the Derivative Actions and/or  
12 the Released Claims, except the Individual Defendants shall not be deemed to have released  
13 Kratos from any claims or causes of action for indemnification, including but not limited to  
14 insurance indemnification, and/or advancement of attorneys’ fees and expenses.

15 As part of the Settlement, within five business days from the date on which the Judgment  
16 approving the Settlement becomes Final, Plaintiffs’ Counsel, on behalf of State Plaintiffs, shall  
17 file a Stipulation of Dismissal with prejudice in the State Action, signed by all parties to the State  
18 Action, and request an order dismissing the State Action. State Plaintiffs shall file and serve  
19 notice of any dismissal order within five business dates of entry by the State Court.

20 As used above, “Effective Date” means the first date by which all the following events  
21 and conditions shall have occurred or been met: (1) execution of the Stipulation; (2) entry of the  
22 Preliminary Approval Order; (3) entry of the Judgment; (4) payments by Kratos and/or its D&O  
23 Insurer(s) in accordance with ¶5.1 of the Stipulation; (5) the Judgment has become Final; and (6)  
24 dismissal of the State Action with prejudice in accordance with ¶8.4 of the Stipulation.

25 As used above, “Individual Defendant Releasees” means Individual Defendants and each  
26 of their past, present, or future directors, officers, employees, partners, insurers, co-insurers,  
27 reinsurers, principals, agents, controlling shareholders, attorneys, accountants or auditors,  
28 advisors, investment advisors, personal or legal representatives, predecessors, successors, parents,

1 subsidiaries, divisions, joint ventures, assigns, spouses, heirs, related or affiliated entities,  
2 immediate family, and any trusts in which Individual Defendant Releasees, or any of them, are  
3 the settlors or which are for the benefit of any Individual Defendant Releasees and/or members of  
4 their/his/her immediate family, and any entities in which Individual Defendants, or any of them,  
5 have a controlling interest (directly or indirectly).

6 As used above, "Kratos Releasees," which does not include Individual Defendant  
7 Releasees, means Kratos and each of its past, present, or future directors, officers, employees,  
8 partners, insurers, co-insurers, reinsurers, principals, agents, controlling shareholders, attorneys,  
9 accountants or auditors, advisors, investment advisors, personal or legal representatives,  
10 predecessors, successors, parents, subsidiaries, divisions, joint ventures, assigns, spouses, heirs,  
11 related or affiliated entities, immediate family, and any trusts in which the Kratos Releasees, or  
12 any of them, are the settlors or which are for the benefit of any Kratos Releasees and/or members  
13 of their/his/her immediate family, and any entities in which Kratos has a controlling interest  
14 (directly or indirectly).

15 As used above, "Plaintiff Releasees" means each of Plaintiffs and each of their past,  
16 present, or future directors, officers, employees, partners, insurers, co-insurers, reinsurers,  
17 principals, agents, controlling shareholders, attorneys, accountants or auditors, advisors,  
18 investment advisors, personal or legal representatives, predecessors, successors, parents,  
19 subsidiaries, divisions, joint ventures, assigns, spouses, heirs, related or affiliated entities,  
20 immediate family, and any trust of which any Plaintiff Releasees, or any of them, are the settlors  
21 or which is for the benefit of any Plaintiff Releasees and/or members of their/his/her immediate  
22 family, and any entity in which Plaintiffs, or any of them, have a controlling interest (directly or  
23 indirectly).

24 As used above, "Released Claims" means any and all claims or causes of action, demands,  
25 rights, liabilities, suits, debts, obligations, and causes of action of every nature and description  
26 whatsoever, known or unknown (including Unknown Claims as defined herein), contingent or  
27 absolute, mature or unmature, discoverable or undiscoverable, whether concealed or hidden  
28 asserted derivatively on behalf of Kratos, or that could have been asserted directly by the Settling

1 Parties, derivatively on behalf of Kratos, or by Kratos itself based upon, arising out of, or related  
2 to the allegations, facts, transactions, or claims in the Derivative Actions, and any claims in  
3 connection with, based upon, or arising out of, or relating to the Settlement.

4 As used above, "Unknown Claims" means any Released Claims that a Person, including  
5 Plaintiffs, may not know or suspect to exist in his, her, or its favor at the time of the release of  
6 Kratos and Individual Defendants which, if known by him, her or it, might have affected his, her  
7 or its settlement and release, or might have affected his, her, or its decision not to object to the  
8 Settlement. With respect to any and all Released Claims, the Settling Parties stipulate and agree  
9 that, upon the Effective Date, Plaintiffs, Kratos Stockholders, and Kratos shall waive and by  
10 operation of the Judgment shall have waived, the provisions, rights, and benefits of California  
11 Civil Code §1542, which provides:

12 **A GENERAL RELEASE DOES NOT EXTEND TO CLAIMS WHICH THE**  
13 **CREDITOR DOES NOT KNOW OR SUSPECT TO EXIST IN HIS OR HER**  
14 **FAVOR AT THE TIME OF EXECUTING THE RELEASE, WHICH IF**  
15 **KNOWN BY HIM OR HER MUST HAVE MATERIALLY AFFECTED HIS**  
16 **SETTLEMENT WITH THE DEBTOR.**

17 Plaintiffs, Kratos Stockholders, and Kratos shall expressly waive, and by operation of the  
18 Judgment shall have expressly waived, any and all provisions, rights and benefits conferred by  
19 any law of any state or territory of the United States, or principle of common law, which is  
20 similar, comparable, or equivalent to California Civil Code §1542. Plaintiffs, Kratos  
21 Stockholders, and Kratos may hereafter discover facts in addition to or different from those which  
22 they now know or believe to be true with respect to the Released Claims, but Plaintiffs, Kratos  
23 Stockholders, and Kratos shall expressly fully, finally, and forever settle and release and, upon  
24 the Effective Date, shall be deemed to have, and by operation of the Judgment shall have, fully,  
25 finally, and forever settled and released, any and all Released Claims, known or unknown,  
26 suspected or unsuspected, contingent or non-contingent, whether or not concealed or hidden,  
27 which now exist, or have existed, upon any theory of law, or equity now existing or coming into  
28 existence in the future, including, but not limited to, conduct which is negligent, intentional, with  
or without malice, or a breach of any duty, law, or rule, without regard to the subsequent  
discovery or existence of such different or additional facts. Plaintiffs acknowledge that the

1 foregoing waiver was separately bargained for and a key element of the Settlement of which this  
2 release is a part.

3 **VII. ATTORNEYS' FEES AND EXPENSE AWARD**

4 Subject to Court approval and in recognition of the benefits conferred on Kratos as a  
5 direct and material factor resulting from the Derivative Actions, Kratos agrees to pay and/or cause  
6 its D&O Insurer(s) to pay to Plaintiffs' Counsel \$2,000,000 (collectively, the "Fees and Expenses  
7 Payment"). The agreed-to Fees and Expenses Payment will compensate Plaintiffs' Counsel for  
8 their efforts in achieving the substantial benefits for Kratos as identified above and in the  
9 Stipulation and for their risk in undertaking this representation on a contingency basis.

10 **VIII. CONDITIONS FOR SETTLEMENT**

11 The Settlement is conditioned upon the occurrence of certain events. Those events  
12 include, among other things: (1) entry of the Judgment by the Court, as provided for in the  
13 Stipulation; and (2) expiration of the time to appeal from or alter or amend the Judgment. If, for  
14 any reason, any one of the conditions described in the Stipulation is not met, the Stipulation might  
15 be terminated and, if terminated, will become null and void, and the parties to the Stipulation will  
16 be restored to their respective positions in the litigation as of January 5, 2010.

17 **IX. THE SETTLEMENT HEARING AND YOUR RIGHTS AS SHAREHOLDERS**

18 The Settlement Hearing shall be held before this Court on \_\_\_\_\_, 20\_\_ at \_\_:\_\_\_  
19 a./p.m. or as soon thereafter as counsel may be heard in the courtroom of the Honorable John A.  
20 Houston of the United States District Court for the Southern District of California, 940 Front  
21 Street, San Diego, CA 92101 to determine: (i) whether the proposed Settlement of the litigation  
22 as set forth in the Stipulation, should be approved in all respects as fair, just, reasonable, and  
23 adequate to, and in the best interests of, Kratos, Kratos Stockholders, and Plaintiffs; (ii) whether  
24 the Final Judgment and Order of Dismissal approving the Settlement should be entered; and (iii)  
25 whether the agreed-to Fees and Expenses Payment should be awarded to Plaintiffs' Counsel. The  
26 Settlement Hearing may be continued or adjourned from time to time by the Court at the  
27 Settlement Hearing or any continued or adjourned session thereof without further notice.  
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Unless otherwise ordered by the Court, any Current Kratos Stockholder who does not make his, her, or its objection or opposition in the manner provided shall be deemed to have waived any and all objections and opposition, and shall be forever foreclosed from making any objection to the fairness, reasonableness, and adequacy of the proposed Settlement, and shall otherwise be bound by the Judgment to be entered and the releases to be given.

**X. EXAMINATION OF PAPERS AND INQUIRES**

This Notice contains only a summary of the terms of the proposed Settlement. For a more detailed statement of the matters involved in this action, reference is made to the pleadings, to the Stipulation and to other papers filed in this action which may be inspected at the Office of the Clerk for the United States District Court for the Southern District of California, 940 Front Street San Diego, CA 92101, during business hours of each business day. In addition, a copy of the Stipulation may be found at [www.kratosdefense.com](http://www.kratosdefense.com).

Inquiries regarding this action should be addressed as follows:

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**DO NOT CONTACT THE COURT REGARDING THIS NOTICE.**

Dated: \_\_\_\_\_

**BY ORDER OF THE COURT  
UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF CALIFORNIA**

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