

KRATOS DEFENSE & SECURITY SOLUTIONS, INC.  
Form 424B5  
August 28, 2009

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Registration No. 333-161340

**PROSPECTUS SUPPLEMENT**  
**(to the Prospectus dated August 21, 2009)**

## **26,000,000 Shares of Common Stock**

We are offering 26,000,000 shares of our common stock to institutional investors pursuant to this prospectus supplement and the accompanying prospectus. The purchase price for each share is \$0.72. Our common stock is traded on the Nasdaq Global Select Market under the symbol "KTOS." On August 27, 2009, the last reported sale price of our common stock on the Nasdaq Global Select Market was \$0.828 per share.

**Investing in our securities involves a high degree of risk. You should review carefully the risks and uncertainties described under the heading "Risk Factors" beginning on page S-4 of this prospectus supplement.**

B. Riley & Co., LLC acted as the placement agent on this transaction. The placement agent is not required to sell any specific number or dollar amount of securities, but has agreed to use its reasonable best efforts to sell the securities offered by this prospectus supplement. We have agreed to pay the placement agent fees set forth in the table below.

	<b>Per Share</b>	<b>Total</b>
Offering price	\$ 0.72	\$ 18,720,000
Placement agent fees	\$ 0.036	\$ 936,000
Proceeds, before expenses, to Kratos Defense & Security Solutions, Inc.	\$ 0.684	\$ 17,784,000

We expect the total offering expenses, excluding placement agent's fees, to be approximately \$160,000 for all sales pursuant to this prospectus supplement and the accompanying prospectus. Because there is no minimum offering amount required as a condition to closing this offering, the actual offering amount, placement agent fees and proceeds to us are not presently determinable and may be substantially less than the maximum amounts set forth above.

Delivery of the shares of common stock offered under this prospectus supplement is expected to be made to investors on or about September 2, 2009.

**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.**

**B. Riley & Co., LLC**

The date of this prospectus supplement is August 28, 2009

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**ABOUT THIS PROSPECTUS SUPPLEMENT**

This document is in two parts. The first part is the prospectus supplement, including the documents incorporated by reference, which describes the specific terms of this offering. The second part, the accompanying prospectus, including the documents incorporated by reference, provides more general information. Generally, when we refer to this prospectus, we are referring to both parts of this document combined. We urge you to carefully read this prospectus supplement and the accompanying prospectus, and the documents incorporated herein and therein, before buying any of the securities being offered under this prospectus supplement. This prospectus supplement may add or update information contained in the accompanying prospectus and the documents incorporated by reference therein. To the extent that any statement that we make in this prospectus supplement is inconsistent with statements made in the accompanying prospectus or any documents incorporated by reference therein that was filed before the date of this prospectus supplement, the statements made in this prospectus supplement will be deemed to modify or supersede those made in the accompanying prospectus and such documents incorporated by reference therein.

You should rely only on the information contained, or incorporated herein by reference, in this prospectus supplement and contained, or incorporated herein by reference, in the accompanying prospectus. We have not authorized anyone to provide you with different information. No dealer, salesperson or other person is authorized to give any information or to represent anything not contained in this prospectus supplement and the accompanying prospectus. You should not rely on any unauthorized information or representation. This prospectus supplement is an offer to sell only the securities offered hereby, and only under circumstances and in jurisdictions where it is lawful to do so. You should assume that the information in this prospectus supplement and the accompanying prospectus is accurate only as of the date on the front of the applicable document and that any information we have incorporated by reference is accurate only as of the date of the document incorporated by reference, regardless of the time of delivery of this prospectus supplement or the accompanying prospectus, or any sale of a security.

Unless otherwise mentioned or unless the context requires otherwise, all references in this prospectus to "the Company," "we," "us," "our," and "Kratos" refer to Kratos Defense & Security Solutions, Inc., a Delaware corporation and its consolidated subsidiaries.

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**PROSPECTUS SUPPLEMENT SUMMARY**

*This summary is not complete and does not contain all of the information that you should consider before investing in the securities offered by this prospectus. You should read this summary together with the entire prospectus supplement and the accompanying prospectus, including our financial statements, the notes to those financial statements and the other documents that are incorporated by reference in this prospectus supplement and the accompanying prospectus, before making an investment decision. See the Risk Factors section of this prospectus supplement beginning on page S-4 for a discussion of the risks involved in investing in our securities.*

**Kratos Defense & Security Solutions, Inc.**

**Our Business**

Kratos Defense & Security Solutions, Inc. is an innovative provider of mission critical engineering, information technology services and warfighter solutions. We work primarily for the U.S. government and federal government agencies, but we also perform work for state and local agencies and commercial customers. Our principal services are related to, but are not limited to, Command, Control, Communications, Computing, Intelligence, Surveillance and Reconnaissance (C4ISR); weapons systems lifecycle support and sustainment; military weapon range operations and technical services; missile, rocket and weapons system test and evaluation; missile and rocket mission launch services; public safety, security and surveillance systems; modeling and simulation; unmanned aerial vehicle products and technology; advanced network engineering and information technology services; and advanced information technology services. We offer our customers solutions and expertise to support their mission-critical needs by leveraging our skills across our core service areas.

We derive a substantial portion of our revenue from contracts performed for federal government agencies, including the U.S. Department of Defense (DOD), with the majority of our revenue currently generated from the delivery of mission-critical warfighter solutions, advanced engineering services, system integration and system sustainment services to defense and other non-DOD and civilian government agencies. We believe our diversified and stable client base, strong client relationships, broad array of contract vehicles, considerable employee base possessing government security clearances, extensive list of past performance qualifications, and significant management and operational capabilities position us for continued growth.

Prior to 2008 we were also an independent provider of outsourced engineering and network deployment services, security systems engineering and integration services and other technical services for the wireless communications industry, the U.S. government and enterprise customers. In 2006 and 2007, we undertook a transformation strategy whereby we divested our commercial wireless-related businesses and chose to pursue business with the federal government, primarily the DOD, through strategic acquisitions. On September 12, 2007, we changed our name from Wireless Facilities, Inc. to Kratos Defense & Security Solutions, Inc. In connection with our name change, we changed our NASDAQ Global Market trading symbol to "KTOS."

**Recent Developments**

As previously disclosed, on June 4, 2009, we filed a complaint in the United States District Court for the Northern District of Ohio against the lenders under our credit agreement, seeking equitable relief in the form of reformation of an error in a contract schedule. The error resulted from the erroneous preparation of a schedule to the loan documents consisting of calculations relating to a financial covenant relating to the minimum liquidity ratio.

On August 27, 2009, we entered into a term sheet, which was negotiated under the jurisdiction of the United States District Court for the Northern District of Ohio, under which the parties intend to

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settle this dispute. The term sheet provides that a definitive settlement agreement will be negotiated and executed on or before September 27, 2009 and, if executed, would effect the reformation of the minimum liquidity ratio in accordance with our request. The term sheet also requires that we use the net proceeds from the sale of the securities under this prospectus supplement to pay down the first term loan at par with no prepayment penalty or make whole payments. The term sheet also provides that we will agree to pay a fee of \$500,000 to our lenders in connection with the execution of a definitive settlement agreement and that the lenders will extend the term of the revolving line of credit by one year to December 31, 2012. In addition, the term sheet provides, among other things, that the parties will execute and deliver mutual releases. The amendments described in this paragraph will not be effective unless and until the parties have executed a definitive settlement agreement, and we can provide no assurance that the definitive settlement agreement will be entered into on the anticipated terms, or at all.

**Our Corporate Information**

We were initially incorporated in the state of New York in 1994, commenced operations in 1995 and were reincorporated in Delaware in 1998. On September 12, 2007, we changed our name from Wireless Facilities, Inc. to Kratos Defense & Security Solutions, Inc. Our executive offices are located at 4810 Eastgate Mall, San Diego, California 92121, and our telephone number is (858) 812-7300. We maintain an Internet website at [www.kratosdefense.com](http://www.kratosdefense.com). Information contained in or accessible through our website does not constitute part of this prospectus supplement or the accompanying prospectus.

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**The Offering**

Common stock offered by us pursuant to this prospectus supplement	26,000,000 shares of common stock
Use of proceeds	We intend to use the net proceeds from the sale of the securities under this prospectus supplement to repay existing indebtedness. To the extent that the net proceeds are not applied to repay existing indebtedness, we intend to use them for general corporate purposes. Pending such uses, the net proceeds will be held in highly liquid investments. See "Use of Proceeds" on page S-22 of this prospectus supplement.
NASDAQ Global Select Market symbol	KTOS
Risk factors	This investment involves a high degree of risk. See "Risk Factors" beginning on page S-4 of this prospectus supplement for a discussion of factors you should carefully consider before deciding to invest in our common stock.

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**RISK FACTORS**

*An investment in our securities involves a substantial risk of loss. You should carefully consider these risk factors, together with all of the other information included or incorporated by reference in this prospectus supplement and the accompanying prospectus, as modified and superseded pursuant to Rule 412 under the Securities Act, before you decide to invest in our common stock. The occurrence of any of the following risks could harm our business. In that case, the trading price of our common stock could decline, and you may lose all or part of your investment. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also impair our operations. You should also refer to the other information contained in this prospectus supplement and the accompanying prospectus or incorporated by reference, including our financial statements and the notes to those statements and the information set forth under the heading "Cautionary Note Regarding Forward-Looking Statements."*

**Risks Related to Our Business**

***Our business could be adversely affected by changes in the contracting or fiscal policies of the federal government and governmental entities.***

We derive a significant portion of our revenue from contracts with the U.S. federal government and government agencies and subcontracts under federal government prime contracts, and the success of our business and growth of our business will continue to depend on our successful procurement of government contracts either directly or through prime contractors. Accordingly, changes in government contracting policies or government budgetary constraints could directly affect our financial performance. Among the factors that could adversely affect our business are:

changes in fiscal policies or decreases in available government funding, including budgetary constraints affecting federal government spending generally, or specific departments or agencies in particular;

the adoption of new laws or regulations or changes to existing laws or regulations;

changes in political or social attitudes with respect to security and defense issues;

changes in federal government programs or requirements, including the increased use of small business providers;

changes in or delays related to government restrictions on the export of defense articles and services;

potential delays or changes in the government appropriations process; and

delays in the payment of our invoices by government payment offices.

These and other factors could cause governments and government agencies, or prime contractors that use us as a subcontractor, to reduce their purchases under existing contracts, to exercise their rights to terminate contracts at-will or to abstain from exercising options to renew contracts, any of which could have an adverse effect on our business, financial condition and results of operations. Many of our government customers are subject to stringent budgetary constraints. The award of additional contracts from government agencies could be adversely affected by spending reductions or budget cutbacks at these agencies.

***Recent deterioration in the credit markets and the financial services industry may negatively impact our business, results of operations, financial condition or liquidity.***

Recently the credit markets and the financial services industry have been experiencing a period of unprecedented turmoil and upheaval characterized by the bankruptcy, failure, collapse or sale of various financial institutions and an unprecedented level of intervention from the United States federal



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government. While the outcome of these events cannot be predicted, they may have an adverse effect on our liquidity, financial condition and results of operations if it became necessary for us to acquire additional debt financing. Given our highly leveraged liquidity position, any down-turn in our operating earnings or cash flows could impair our ability to comply with the financial covenants of our existing credit facility. If additional debt financing were required, it may be at interest rates far greater than our current outstanding debt or may not be available at all.

Although we maintain allowances for doubtful accounts for estimated losses from the inability of our customers to make required payments and such losses have historically been within our expectations and the allowances we have established, we cannot guarantee that we will continue to experience the same loss rates we have in the past, especially given the recent deterioration of the credit markets. A significant change in the liquidity or financial condition of our customers could cause unfavorable trends in our revenue and receivable collections and additional allowances may be required. These additional allowances could materially affect our financial results.

***Our ability to make payments on our debt will be contingent on our future operating performance, which will depend on a number of factors that are outside our control.***

Our debt service obligations are estimated to be approximately \$11.0 million to \$13.0 million in 2009, including approximately \$5.9 million of principal repayments. This debt service may have an adverse impact on our earnings and cash flow, which could in turn negatively impact our stock price.

Our ability to make principal and interest payments on our debt is contingent on our future operating performance, which will depend on a number of factors, many of which are outside of our control. The degree to which we are leveraged could have other important negative consequences, including the following:

we must dedicate a substantial portion of our cash flows from operations to the payment of our indebtedness, reducing the funds available for future working capital requirements, capital expenditures, acquisitions or other general corporate requirements;

a significant portion of our borrowings are, and will continue to be, at variable rates of interest, which may result in higher interest expense in the event of increases in interest rates;

we may be more vulnerable to a downturn in the industries in which we operate or a downturn in the economy;

we may be limited in our flexibility to plan for, or react to, changes in our business and the industries in which we operate;

we may be placed at a competitive disadvantage compared to our competitors that have less debt;

we may determine it to be necessary to dispose of certain assets or one or more of our businesses to reduce our debt; and

our ability to borrow additional funds in excess of our current financing may be limited.

Our business may not generate sufficient cash flow from operations and future borrowings may not be available in amounts sufficient to enable us to pay our indebtedness or fund our other liquidity needs. Moreover, we may need to refinance all or a portion of our indebtedness on or before maturity. In such a case, we may not be able to refinance any of our indebtedness on commercially reasonable terms or at all. If we are unable to make scheduled debt payments or comply with the other provisions of our debt instruments, our lenders may be permitted under certain circumstances to accelerate the maturity of the indebtedness owed to them and exercise other remedies provided for in those instruments and under applicable law.



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***We have incurred and may continue to incur goodwill impairment charges in our reporting entities which could harm our profitability.***

A significant portion of our net assets come from goodwill and other intangible assets. In accordance with Statement of Financial Accounting Standards, or SFAS 142, "Goodwill and Other Intangible Assets," (SFAS 142) we periodically review the carrying values of our goodwill to determine whether such carrying values exceed the fair market value. Our acquired companies are subject to annual review for goodwill impairment. If impairment testing indicates that the carrying value of a reporting unit exceeds its fair value, the goodwill of the reporting unit is deemed impaired. Accordingly, an impairment charge would be recognized for that reporting unit in the period identified. In 2008, as a result of our annual review, we recorded a goodwill impairment charge of \$105.8 million related to our KGS segment, to reflect the declining market and economic conditions through December 28, 2008.

Given the continued significant decline in the stock market in general and specifically the impact on our stock price in 2009, we performed an impairment test for goodwill in accordance with SFAS 142 as of February 28, 2009. The test indicated that the book value for the KGS segment exceeded the fair values of the businesses and resulted in our recording a charge totaling \$41.3 million in our KGS segment for the impairment of goodwill. The impairment charge is primarily driven by adverse equity market conditions that caused a decrease in current market multiples and our average stock price as of February 28, 2009, compared with the test performed as of December 28, 2008.

***We derive a substantial amount of our revenues from the sale of our solutions either directly or indirectly to U.S. government entities pursuant to government contracts, which differ materially from standard commercial contracts, involve competitive bidding and may be subject to cancellation or delay without penalty, any of which may produce volatility in our revenues and earnings.***

Government contracts frequently include provisions that are not standard in private commercial transactions, and are subject to laws and regulations that give the federal government rights and remedies not typically found in commercial contracts, including provisions permitting the federal government to:

terminate our existing contracts;

reduce potential future income from our existing contracts;

modify some of the terms and conditions in our existing contracts;

suspend or permanently prohibit us from doing business with the federal government or with any specific government agency;

impose fines and penalties;

subject us to criminal prosecution;

suspend work under existing multiple year contracts and related task orders if the necessary funds are not appropriated by Congress;

decline to exercise an option to extend an existing multiple year contract; and

claim rights in technologies and systems invented, developed or produced by us.

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In addition, government contracts are frequently awarded only after formal competitive bidding processes, which have been and may continue to be protracted and typically impose provisions that permit cancellation in the event that necessary funds are unavailable to the public agency. Competitive procurements impose substantial costs and managerial time and effort in order to prepare bids and proposals for contracts that may not be awarded to us. In many cases, unsuccessful bidders for

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government agency contracts are provided the opportunity to formally protest certain contract awards through various agencies, administrative and judicial channels. The protest process may substantially delay a successful bidder's contract performance, result in cancellation of the contract award entirely and distract management. We may not be awarded contracts for which we bid, and substantial delays or cancellation of purchases may follow our successful bids as a result of such protests.

Certain of our government contracts also contain "organizational conflict of interest" clauses that could limit our ability to compete for certain related follow-on contracts. For example, when we work on the design of a particular solution, we may be precluded from competing for the contract to install that solution. While we actively monitor our contracts to avoid these conflicts, we cannot guarantee that we will be able to avoid all organizational conflict of interest issues.

***We may not receive the full amounts estimated under the contracts in our backlog, which could reduce our revenue in future periods below the levels anticipated and which makes backlog an uncertain indicator of future operating results.***

As of June 28, 2009, our backlog was approximately \$640 million, of which \$130 million was funded. Funded backlog is estimated future revenue under government contracts and task orders for which funding has been appropriated by Congress and authorized for expenditure by the applicable agency, plus our estimate of the future revenue we expect to realize from our commercial contracts that are under firm orders. Although funded backlog represents only business which is considered to be firm, cancellations or scope adjustments may still occur. The remaining \$510 million is unfunded backlog, which reflects our estimate of future revenue under awarded government contracts and task orders for which either funding has not yet been appropriated or expenditure has not yet been authorized. Unfunded backlog does not include estimates of revenue from GWAC contracts or GSA schedules beyond awarded or funded task orders, but does include estimates of revenue beyond awarded or funded task orders for other types of IDIQ contracts. The amount of unfunded backlog is not exact or guaranteed and is based upon, among other things, management's experience under such contracts and similar contracts, the particular clients, the type of work and budgetary expectations. Our management may not accurately assess these factors or estimate the revenue we will realize from these contracts, and our unfunded and total backlog may not reflect the actual revenue ultimately received from these contracts.

Backlog is typically subject to large variations from quarter to quarter and comparisons of backlog from period to period are not necessarily indicative of future revenues. The contracts comprising our backlog may not result in actual revenue in any particular period or at all, and the actual revenue from such contracts may differ from our backlog estimates. The timing of receipt of revenues, if any, on projects included in backlog could change because many factors affect the scheduling of projects. Cancellation of or adjustments to contracts may occur. Additionally, all United States government contracts included in backlog, whether or not funded, may be terminated at the convenience of the United States government. The failure to realize all amounts in our backlog could adversely affect our revenues and gross margins. As a result, our funded and total backlog as of any particular date may not be an accurate indicator of our future earnings.

***We face intense competition from many competitors that have greater resources than we do, which could result in price reductions, reduced profitability or loss of market share.***

We operate in highly competitive markets and generally encounter intense competition to win contracts from many other firms, including mid-tier federal contractors with specialized capabilities and large defense and IT services providers. Competition in our markets may increase as a result of a number of factors, such as the entrance of new or larger competitors, including those formed through alliances or consolidation. These competitors may have greater financial, technical, marketing and

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public relations resources, larger client bases and greater brand or name recognition than we do. These competitors could, among other things:

divert sales from us by winning very large-scale government contracts, a risk that is enhanced by the recent trend in government procurement practices to bundle services into larger contracts;

force us to charge lower prices; or

adversely affect our relationships with current clients, including our ability to continue to win competitively awarded engagements in which we are the incumbent.

If we lose business to our competitors or are forced to lower our prices, our revenue and our operating profits could decline. In addition, we may face competition from our subcontractors who, from time-to-time, seek to obtain prime contractor status on contracts for which they currently serve as a subcontractor to us. If one or more of our current subcontractors are awarded prime contractor status on such contracts in the future, it could divert sales from us or could force us to charge lower prices, which could cause our margins to suffer.

***Recent acquisitions and potential future acquisitions could prove difficult to integrate, disrupt our business, dilute stockholder value and strain our resources.***

We have completed several acquisitions of complementary businesses in recent years, including our December 2007 acquisition of Haverstick Consulting, Inc., our June 2008 acquisition of SYS, and our December 2008 acquisition of DFI. The success of the acquisitions will depend in part on the success of integrating the operations, technologies and personnel of SYS and DFI. The failure to successfully integrate the operations of the two companies or otherwise to realize any of the anticipated benefits of the acquisitions could seriously harm our results of operations.

We continually evaluate opportunities to acquire new businesses as part of our ongoing strategy and we may in the future acquire additional companies that we believe could complement or expand our business or increase our customer base. Acquisitions involve numerous risks, including:

difficulties in integrating operations, technologies, accounting and personnel;

difficulties in supporting and transitioning customers of acquired companies;

difficulties or delays in transitioning federal government contracts pursuant to federal acquisition regulations;

diversion of financial and management resources from existing operations;

potential loss of key employees;

federal acquisition regulations may require us to enter into government novation agreements, a potentially time-consuming process; and

inability to generate sufficient revenue to offset acquisition costs.

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Acquired companies may have liabilities or adverse operating issues that we fail to discover through due diligence prior to the acquisition. In particular, to the extent that prior owners of any acquired businesses or properties failed to comply with or otherwise violated applicable laws or regulations, or failed to fulfill their contractual obligations to the federal government or other clients, we, as the successor owner, may be financially responsible for these violations and failures and may suffer reputational harm or otherwise be adversely affected. Acquisitions also frequently result in the recording of goodwill and other intangible assets which are subject to potential impairments in the future that could harm our financial results. In addition, if we finance acquisitions by issuing convertible debt or equity securities, our existing stockholders may be diluted, which could affect the market price of our stock. As a result, if we fail to properly evaluate acquisitions or investments, we

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may not achieve the anticipated benefits of any such acquisitions, and we may incur costs in excess of what we anticipate.

***Our financial results may vary significantly from quarter to quarter.***

We expect our revenue and operating results to vary from quarter to quarter. Reductions in revenue in a particular quarter could lead to lower profitability in that quarter because a relatively large amount of our expenses are fixed in the short-term. We may incur significant operating expenses during the start-up and early stages of large contracts and may not be able to recognize corresponding revenue in that same quarter. We may also incur additional expenses when contracts expire, are terminated or are not renewed.

In addition, payments due to us from federal government agencies may be delayed due to billing cycles or as a result of failures of government budgets to gain congressional and administration approval in a timely manner. The federal government's fiscal year ends September 30. If a federal budget for the next federal fiscal year has not been approved by that date in each year, our clients may have to suspend engagements that we are working on until a budget has been approved. Any such suspensions may reduce our revenue in the fourth quarter of that year or the first quarter of the subsequent year. The federal government's fiscal year end can also trigger increased purchase requests from clients for equipment and materials. Any increased purchase requests we receive as a result of the federal government's fiscal year end would serve to increase our third or fourth quarter revenue, but will generally decrease profit margins for that quarter, as these activities generally are not as profitable as our typical offerings.

Additional factors that may cause our financial results to fluctuate from quarter to quarter include those addressed elsewhere in these Risk Factors and the following, among others:

the terms of customer contracts that affect the timing of revenue recognition;

variability in demand for our services and solutions;

commencement, completion or termination of contracts during any particular quarter;

timing of award or performance incentive fee notices;

timing of significant bid and proposal costs;

variable purchasing patterns under GSA Schedule 70 contracts, government wide acquisition contracts (GWACs), blanket purchase agreements and other indefinite delivery/indefinite quantity contracts;

restrictions on and delays related to the export of defense articles and services;

costs related to ongoing government inquiries;

strategic decisions by us or our competitors, such as acquisitions, divestitures, spin-offs and joint ventures;

strategic investments or changes in business strategy;

changes in the extent to which we use subcontractors;

seasonal fluctuations in our staff utilization rates;

changes in our effective tax rate including changes in our judgment as to the necessity of the valuation allowance recorded against our deferred tax assets; and

the length of sales cycles.

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Significant fluctuations in our operating results for a particular quarter could cause us to fall out of compliance with the financial covenants contained in our credit facility, which if not waived by the lender, could restrict our access to capital and cause us to take extreme measures to pay down our debt under the credit facility. In addition, fluctuations in our financial results could cause our stock price to decline.

***If we fail to establish and maintain important relationships with government entities and agencies and other government contractors, our ability to bid successfully for new business may be adversely affected.***

To develop new business opportunities, we primarily rely on establishing and maintaining relationships with various government entities and agencies. We may be unable to successfully maintain our relationships with government entities and agencies, and any failure to do so could materially adversely affect our ability to compete successfully for new business. In addition, we often act as a subcontractor or in "teaming" arrangements in which we and other contractors bid together on particular contracts or programs for the federal government or government agencies. As a subcontractor or team member, we often lack control over fulfillment of a contract, and poor performance on the contract could tarnish our reputation, even when we perform as required. We expect to continue to depend on relationships with other contractors for a portion of our revenue in the foreseeable future. Moreover, our revenue and operating results could be materially adversely affected if any prime contractor or teammate chooses to offer a client services of the type that we provide or if any prime contractor or teammate teams with other companies to independently provide those services.

***We derive a significant portion of our revenues from a limited number of customers.***

We have derived, and believe that we will continue to derive, a significant portion of our revenues from a limited number of customers. To the extent that any significant customer uses less of our services or terminates its relationship with us, our revenues could decline significantly. As a result, the loss of any significant client could seriously harm our business. For the three and six months ended June 28, 2009, two customers comprised approximately 63% and 62% of our federal business revenues and total revenues, respectively, and our five largest customers accounted for approximately 75% and 74% of our total federal business revenues and total revenues, respectively. None of our customers are obligated to purchase additional services from us. As a result, the volume of work that we perform for a specific customer is likely to vary from period to period, and a significant client in one period may not use our services in a subsequent period.

***Our margins and operating results may suffer if we experience unfavorable changes in the proportion of cost-plus-fee or fixed-price contracts in our total contract mix.***

Although fixed-price contracts entail a greater risk of a reduced profit or financial loss on a contract compared to other types of contracts we enter into, fixed-price contracts typically provide higher profit opportunities because we may be able to benefit from cost savings. In contrast, cost-plus-fee contracts are subject to statutory limits on profit margins, and generally are the least profitable of our contract types. Our federal government customers typically determine what type of contract we enter into. Cost-plus-fee and fixed-price contracts in our federal business accounted for approximately 34% and 32%, respectively, of our federal business revenues for the six months ended June 28, 2009. To the extent that we enter into more cost-plus-fee or less fixed-price contracts in proportion to our total contract mix in the future, our margins and operating results may suffer.

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***Our cash flow and profitability could be reduced if expenditures are incurred prior to the final receipt of a contract.***

We provide various professional services and sometimes procure equipment and materials on behalf of our federal government customers under various contractual arrangements. From time to time, in order to ensure that we satisfy our customers' delivery requirements and schedules, we may elect to initiate procurement in advance of receiving final authorization from the government customer or a prime contractor. If our government or prime contractor customers' requirements should change or if the government or the prime contractor should direct the anticipated procurement to a contractor other than us or if the equipment or materials become obsolete or require modification before we are under contract for the procurement, our investment in the equipment or materials might be at risk if we cannot efficiently resell them. This could reduce anticipated earnings or result in a loss, negatively affecting our cash flow and profitability.

***Loss of our GSA contracts or GWACs would impair our ability to attract new business.***

We are a prime contractor under several GSA contracts and GWAC schedule contracts. We believe that our ability to provide services under these contracts will continue to be important to our business because of the multiple opportunities for new engagements each contract provides. If we were to lose our position as prime contractor on one or more of these contracts, we could lose substantial revenues and our operating results could suffer. GSA contracts and other GWACs typically have a one or two-year initial term with multiple options exercisable at the government client's discretion to extend the contract for one or more years. We cannot be assured that our government clients will continue to exercise the options remaining on our current contracts, nor can we be assured that our future clients will exercise options on any contracts we may receive in the future.

***Failure to properly manage projects may result in additional costs or claims.***

Our engagements often involve large scale, highly complex projects. The quality of our performance on such projects depends in large part upon our ability to manage the relationship with our customers, and to effectively manage the project and deploy appropriate resources, including third-party contractors, and our own personnel, in a timely manner. Any defects or errors or failure to meet clients' expectations could result in claims for substantial damages against us. Our contracts generally limit our liability for damages that arise from negligent acts, error, mistakes or omissions in rendering services to our clients. However, we cannot be sure that these contractual provisions will protect us from liability for damages in the event we are sued. In addition, in certain instances, we guarantee customers that we will complete a project by a scheduled date. If the project experiences a performance problem, we may not be able to recover the additional costs we will incur, which could exceed revenues realized from a project. Finally, if we underestimate the resources or time we need to complete a project with capped or fixed fees, our operating results could be seriously harmed.

***The loss of any member of our senior management could impair our relationships with federal government clients and disrupt the management of our business.***

We believe that the success of our business and our ability to operate profitably depends on the continued contributions of the members of our senior management. We rely on our senior management to generate business and execute programs successfully. In addition, the relationships and reputation that many members of our senior management team have established and maintain with federal government personnel contribute to our ability to maintain strong client relationships and to identify new business opportunities. We do not have any employment agreements providing for a specific term of employment with any member of our senior management. The loss of any member of our senior management could impair our ability to identify and secure new contracts, to maintain good client relations and to otherwise manage our business.

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***If we fail to attract and retain skilled employees or employees with the necessary security clearances, we might not be able to perform under our contracts or win new business.***

The growth of our business and revenue depends in large part upon our ability to attract and retain sufficient numbers of highly qualified individuals who have advanced information technology and/or engineering skills. These employees are in great demand and are likely to remain a limited resource in the foreseeable future. Certain federal government contracts require us, and some of our employees, to maintain security clearances. Obtaining and maintaining security clearances for employees involves a lengthy process, and it is difficult to identify, recruit and retain employees who already hold security clearances. In addition, some of our contracts contain provisions requiring us to staff an engagement with personnel that the client considers key to our successful performance under the contract. In the event we are unable to provide these key personnel or acceptable substitutions, the client may terminate the contract and we may lose revenue.

If we are unable to recruit and retain a sufficient number of qualified employees, our ability to maintain and grow our business could be limited. In a tight labor market, our direct labor costs could increase or we may be required to engage large numbers of subcontractor personnel, which could cause our profit margins to suffer. Conversely, if we maintain or increase our staffing levels in anticipation of one or more projects and the projects are delayed, reduced or terminated, we may underutilize the additional personnel, which would increase our general and administrative expenses, reduce our earnings and possibly harm our results of operations.

***If our subcontractors fail to perform their contractual obligations, our performance and reputation as a prime contractor and our ability to obtain future business could suffer.***

As a prime contractor, we often rely upon other companies to perform work we are obligated to perform for our clients as subcontractors. As we secure more work under our GWAC vehicles, we expect to require an increasing level of support from subcontractors that provide complementary and supplementary services to our offerings. Depending on labor market conditions, we may not be able to identify, hire and retain sufficient numbers of qualified employees to perform the task orders we expect to win. In such cases, we will need to rely on subcontracts with unrelated companies. Moreover, even in favorable labor market conditions, we anticipate entering into more subcontracts in the future as we expand our work under our GWACs. We are responsible for the work performed by our subcontractors, even though in some cases we have limited involvement in that work.

If one or more of our subcontractors fail to satisfactorily perform the agreed-upon services on a timely basis or violate federal government contracting policies, laws or regulations, our ability to perform our obligations as a prime contractor or meet our clients' expectations may be compromised. In extreme cases, performance or other deficiencies on the part of our subcontractors could result in a client terminating our contract for default. A termination for default could expose us to liability, including liability for the agency's costs of procurement, could damage our reputation and could hurt our ability to compete for future contracts.

***Our failure to comply with complex procurement laws and regulations could cause us to lose business and subject us to a variety of penalties.***

We must comply with laws and regulations relating to the formation, administration and performance of federal government contracts, which affect how we do business with our clients, prime contractors, subcontractors and vendors and may impose added costs on us. In addition, the federal government, including the Defense Contract Audit Agency (DCAA), audits and reviews our performance on contracts, pricing practices, cost structure and compliance with applicable laws, regulations and standards. The DCAA reviews a contractor's internal control systems and policies, including the contractor's purchasing, property, estimating, compensation and management information

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systems, and the contractor's compliance with such policies. Any costs found to be improperly allocated to a specific contract will not be reimbursed, while such costs already reimbursed must be refunded. Adverse findings in a DCAA audit could materially affect our competitive position and result in a substantial adjustment to our revenue and profit.

If a federal government audit uncovers improper or illegal activities, we may be subject to civil and criminal penalties and administrative sanctions, including termination of contracts, forfeiture of profits, suspension of payments, fines and suspension or debarment from doing business with federal government agencies. In addition, we could suffer serious harm to our reputation and competitive position if allegations of impropriety were made against us, whether or not true. If our reputation or relationship with federal government agencies were impaired, or if the federal government otherwise ceased doing business with us or significantly decreased the amount of business it does with us, our revenue and operating profit would decline.

***The commercial business arena in which we operate has relatively low barriers to entry and increased competition could result in margin erosion, which would make profitability even more difficult to sustain.***

Other than the technical skills required in our commercial business, the barriers to entry in this area are relatively low. We do not have any intellectual property rights in this segment of our business to protect our methods, and business start-up costs do not pose a significant barrier to entry. The success of our commercial business is dependent on our employees, customer relations and the successful performance of our services. If we face increased competition as a result of new entrants in our markets, we could experience reduced operating margins and loss of market share and brand recognition.

***If our commercial customers do not invest in security systems and other new in-building technologies such as wireless local area networks and/or IP-based networks, our business will suffer.***

We intend to devote significant resources to developing our enterprise-based wireless local area networks (WLAN), but we cannot predict that we will achieve widespread market acceptance amongst the enterprises we identify as potential customers. It is possible that some enterprises will determine that capital constraints and other factors outweigh their need for WLAN systems. As a result, we may be affected by a significant delay in the adoption of WLAN by enterprises, which would harm our business.

***If we experience systems or service failure, our reputation could be harmed and our clients could assert claims against us for damages or refunds.***

We create, implement and maintain IT solutions that are often critical to our clients' operations. We have experienced, and may in the future experience, some systems and service failures, schedule or delivery delays and other problems in connection with our work. If we experience these problems, we may:

lose revenue due to adverse client reaction;

be required to provide additional services to a client at no charge;

receive negative publicity, which could damage our reputation and adversely affect our ability to attract or retain clients; and

suffer claims for substantial damages.

In addition to any costs resulting from product or service warranties, contract performance or required corrective action, these failures may result in increased costs or loss of revenue if clients postpone subsequently scheduled work or cancel, or fail to renew, contracts.

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While many of our contracts limit our liability for consequential damages that may arise from negligence in rendering services to our clients, we cannot assure you that these contractual provisions will be legally sufficient to protect us if we are sued. In addition, our errors and omissions and product liability insurance coverage may not be adequate, may not continue to be available on reasonable terms or in sufficient amounts to cover one or more large claims, or the insurer may disclaim coverage as to some types of future claims. The successful assertion of any large claim against us could seriously harm our business. Even if not successful, these claims could result in significant legal and other costs, may be a distraction to our management and may harm our reputation.

***Security breaches in sensitive federal government systems could result in the loss of clients and negative publicity.***

Many of the systems we develop, install and maintain involve managing and protecting information involved in intelligence, national security and other sensitive or classified federal government functions. A security breach in one of these systems could cause serious harm to our business, damage our reputation and prevent us from being eligible for further work on sensitive or classified systems for federal government clients. We could incur losses from such a security breach that could exceed the policy limits under our errors and omissions and product liability insurance. Damage to our reputation or limitations on our eligibility for additional work resulting from a security breach in one of the systems we develop, install and maintain could materially reduce our revenue.

***Our employees may engage in misconduct or other improper activities, which could cause us to lose contracts.***

We are exposed to the risk that employee fraud or other misconduct could occur. Misconduct by employees could include intentional failures to comply with federal government procurement regulations, engaging in unauthorized activities or falsifying time records. Employee misconduct could also involve the improper use of our clients' sensitive or classified information, which could result in regulatory sanctions against us and serious harm to our reputation and could result in a loss of contracts and a reduction in revenues. It is not always possible to deter employee misconduct, and the precautions we take to prevent and detect this activity may not be effective in controlling unknown or unmanaged risks or losses, which could cause us to lose contracts or cause a reduction in revenues. In addition, alleged or actual employee misconduct could result in investigations or prosecutions of employees engaged in the subject activities, which could result in unanticipated consequences or expenses and management distraction for us regardless of whether we are alleged to have any responsibility.

***Our business is dependent upon our ability to keep pace with the latest technological changes.***

The market for our services is characterized by rapid change and technological improvements. Failure to respond in a timely and cost effective way to these technological developments would result in serious harm to our business and operating results. We have derived, and we expect to continue to derive, a substantial portion of our revenues from providing innovative engineering services and technical solutions that are based upon today's leading technologies and that are capable of adapting to future technologies. As a result, our success will depend, in part, on our ability to develop and market service offerings that respond in a timely manner to the technological advances of our customers, evolving industry standards and changing client preferences.

***If we are unable to manage our growth, our business could be adversely affected.***

Sustaining our growth has placed significant demands on our management, as well as on our administrative, operational and financial resources. For us to continue to manage our growth, we must continue to improve our operational, financial and management information systems and expand, motivate and manage our workforce. If we are unable to manage our growth while maintaining our

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quality of service and profit margins, or if new systems that we implement to assist in managing our growth do not produce the expected benefits, our business, prospects, financial condition or operating results could be adversely affected.

***We may be harmed by intellectual property infringement claims and our failure to protect our intellectual property could enable competitors to market products and services with similar features.***

We may become subject to claims from our employees or third parties who assert that software and other forms of intellectual property that we use in delivering services and solutions to our clients infringe upon intellectual property rights of such employees or third parties. Our employees develop some of the software and other forms of intellectual property that we use to provide our services and solutions to our clients, but we also license technology from other vendors. If our employees, vendors, or other third parties assert claims that we or our clients are infringing on their intellectual property rights, we could incur substantial costs to defend those claims. If any of these infringement claims are ultimately successful, we could be required to cease selling or using products or services that incorporate the challenged software or technology, obtain a license or additional licenses from our employees, vendors, or other third parties, or redesign our products and services that rely on the challenged software or technology.

We attempt to protect our trade secrets by entering into confidentiality and intellectual property assignment agreements with third parties, our employees and consultants. However, these agreements can be breached and, if they are, there may not be an adequate remedy available to us. In addition, others may independently discover our trade secrets and proprietary information and in such cases we could not assert any trade secret rights against such party. Enforcing a claim that a party illegally obtained and is using our trade secret is difficult, expensive and time consuming, and the outcome is unpredictable. If we are unable to protect our intellectual property, our competitors could market services or products similar to our services and products, which could reduce demand for our offerings. Any litigation to enforce our intellectual property rights, protect our trade secrets or determine the validity and scope of the proprietary rights of others could result in substantial costs and diversion of resources, with no assurance of success.

***The matters relating to our internal review of our stock option granting practices and the restatement of our financial statements have exposed us to civil litigation claims, regulatory proceedings and government proceedings, which could have a material adverse effect on us.***

In the summer of 2006, our current executive management team, which has been in place since 2004, initiated an investigation of our past stock option granting practices (the "Equity Award Review") in reaction to media reports regarding stock option granting practices of public companies. The Equity Award Review was conducted with oversight from the Board and assistance from our outside counsel. In February 2007, the Board appointed a Special Committee of the Board to review the adequacy of the Equity Award Review and the recommendations of management regarding historical option granting practices, and to make recommendations and findings regarding those practices and individual conduct. The Special Committee was not charged with making, and did not make, any evaluation of the accounting determinations or tax adjustments. The Special Committee was comprised of a non-employee director who had not served on our Compensation Committee before 2005.

The Equity Award Review encompassed all grants of options to purchase shares of our common stock and other equity awards made since two months prior to our IPO in November 1999 through December 2006. We also reviewed all option grants that were entered into our stock option database (Equity Edge) after our IPO with a grant date before November 1999, as well as other substantial grants issued prior to our IPO, consisting of more than 14,000 grants. We further reviewed all option grants with a grant date that preceded an employee's date of hire. As part of the review, interviews of 18 current and former officers, directors, employees and attorneys were conducted, and more than

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40 million pages of electronic and hard copy documents were searched for relevant information. The Special Committee also conducted its own separate review of the option granting practices during the tenure of current executive management team through additional interviews and document collection and review with the assistance of its own separate counsel and FTI Consulting.

The Equity Award Review established the absence of contemporaneous evidence supporting a substantial number of the previously-recorded option grants, substantially all of which were made in the period from 1998 through late 2003. During this period of time, in some instances, documents, data and interviews suggest that option grants were prepared or finalized days or, in some cases, weeks or months after the option grant date recorded in our books. The affected grants include options issued to certain newly-hired employees but dated prior to their employment start dates and options issued to non-employees, including advisors to the Board erroneously designated as employees. The Special Committee also concluded that certain former employees and former officers participated in making improper option grants, including the selection of grant dates with the benefit of hindsight and in the deferral of the recording of otherwise approved option grants.

In light of the Equity Award Review, the Audit Committee of our Board concluded that our prior financial statements for periods from 1998 through our filing of interim financial statements for the period ended September 30, 2006, could no longer be relied upon and must be restated. Our management determined that, from fiscal year 1998 through fiscal year 2005, we had unrecorded non-cash equity-based compensation charges associated with our equity incentive plans. These charges are material to our financial statements for the years ended December 31, 1998 through 2005, the periods to which such charges would have related. Previously filed annual reports on Form 10-K and quarterly reports on Form 10-Q affected by the restatements have not been and will not be amended and should not be relied upon. Our Annual Report on Form 10-K filed on September 11, 2007 superseded and replaced in their entirety all of our previously issued financial statements and related reports filed with the Securities and Exchange Commission.

Our past stock option granting practices and the restatement of our prior financial statements have exposed and may continue to expose us to greater risks associated with litigation, regulatory proceedings and government inquiries and enforcement actions. As described in Part I, Item 3, "Legal Proceedings," several derivative complaints have been filed in state and federal courts against our current directors, some of our former directors and some of our current and former executive officers pertaining to allegations relating to stock option grants. The SEC initiated an inquiry into our historical stock option granting practices, and we received a subpoena from the United States Attorney's Office for the Southern District of California for the production of documents relating to our historical stock option granting practices.

In April 2008, the SEC notified us that it had completed its investigation and that it did not intend to recommend any enforcement action by the SEC against us. We have cooperated and expect to continue to cooperate with the U.S. Attorney's Office. The period of time necessary to resolve the U.S. Attorney's Office inquiry is uncertain, and we cannot predict the outcome of this inquiry or whether we will face additional government inquiries, investigations or other actions related to our historical stock option grant practices. Subject to certain limitations, we are obligated to indemnify our current and former directors, officers and employees in connection with the investigation of our historical stock option practices, the completed SEC and pending U.S. Attorney's Office inquiries and any future government inquiries, investigations or actions. These inquiries could require us to expend significant management time and incur significant legal and other expenses, and could result in civil and criminal actions seeking, among other things, injunctions against us and the payment of significant fines and penalties by us, which could have a material adverse effect on our financial condition, business, results of operations and cash flow.

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If a federal government investigation uncovers improper or illegal activities, including any potential improper or illegal activities related to our stock option review or related matters, we may be subject to civil and criminal penalties and administrative sanctions, including termination of contracts, forfeiture of profits, suspension of payments, fines and suspension or debarment from doing business with federal government agencies. The aggregate and ongoing legal fees associated with the investigation and defense of the matters related to the Equity Award Review are significant, but the impact has been partially mitigated by funds available under insurance policies purchased in prior years. We cannot assure you that the insurers will continue to reimburse us for ongoing fees. Moreover, the insurance policies contain a number of provisions that the insurers could assert either to discontinue payments or even to seek the return of previously made payments. For instance, if it were determined by final adjudication in the underlying action or in a separate action or proceeding that former officers or directors committed deliberate fraudulent or criminal acts, then insurers could assert that coverage under our directors and officer's liability insurance policies for those periods could be rescinded. In the event of such a determination and an assertion by an insurer, the insurance carriers could pursue a claim against the former officers and directors and/or us for amounts previously advanced under the underlying policies. If insurance coverage is withheld or rescinded by our insurance carriers, we could be exposed to potentially significant financial burdens arising from continuing to fund ongoing costs and costs associated with potential claims for return of prior payments, which could cause us significant harm. In addition, we could suffer serious harm to our reputation and competitive position if allegations of impropriety were made against us, whether or not true. If our reputation or relationship with federal government agencies were impaired, or if the federal government otherwise ceased doing business with us or significantly decreased the amount of business it does with us, our revenue and operating profit would decline.

***If we fail to maintain an effective system of internal controls, we may not be able to accurately report our financial results or prevent fraud.***

Effective internal controls are necessary for us to provide reliable financial reports. If we cannot provide reliable financial reports, our operating results could be misstated, our reputation may be harmed and the trading price of our stock could be negatively affected. Our management has concluded that there are no material weaknesses in our internal controls over financial reporting as of December 28, 2008. However, there can be no assurance that our controls over financial processes and reporting will be effective in the future or that additional material weaknesses or significant deficiencies in our internal controls will not be discovered in the future. Any failure to remediate any future material weaknesses or implement required new or improved controls, or difficulties encountered in their implementation, could harm our operating results, cause us to fail to meet our reporting obligations or result in material misstatements in our financial statements or other public disclosures. Inferior internal controls could also cause investors to lose confidence in our reported financial information, which could have a negative effect on the trading price of our stock. In addition, from time to time we acquire businesses which could have limited infrastructure and systems of internal controls.

On June 28, 2008, we completed the acquisition of SYS and on December 24, 2008, we completed the acquisition of DFI and, as permitted by SEC guidance, we excluded from our assessment of the effectiveness of our internal control over financial reporting as of December 28, 2008, the internal control over financial reporting of these two entities. These operations will be included in our assessment of internal controls over financial reporting for the year ending December 27, 2009. Performing assessments of internal controls, implementing necessary changes, and maintaining an effective internal controls process is costly and requires considerable management attention, particularly in the case of newly acquired entities.

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***We may need additional capital in the future to fund the growth of our business, and financing may not be available.***

We currently anticipate that our available capital resources, including our credit facility and operating cash flows, will be sufficient to meet our expected working capital and capital expenditure requirements for at least the next 12 months. However, such resources may not be sufficient to fund the long-term growth of our business or the expenses associated with the ongoing litigation, litigation settlements and government inquiries. In particular, we may experience a negative operating cash flow due to billing milestones and project timelines in certain of our contracts.

We may raise additional funds through public or private debt or equity financings if such financings become available on favorable terms or we may expand our credit facility to fund future acquisitions and for general corporate purposes. However, due to the current challenges in the lending markets, we can provide no assurance that the lender would agree to extend additional or continuing credit under that facility. We could fall out of compliance with financial and other covenants contained in our credit facility which, if not waived, would restrict our access to capital and could require us to pay down our existing debt under the credit facility. Any new financing or offerings would likely dilute our stockholders' equity ownership. In addition, additional financing may not be available on terms favorable to us, or at all. If adequate funds are not available or are not available on acceptable terms, we may not be able to take advantage of available opportunities, develop new products or otherwise respond to competitive pressures. In any such case, our business, operating results or financial condition could be materially adversely affected.

***We are subject to restrictive debt covenants pursuant to our indebtedness. These covenants may restrict our ability to finance our business and, if we do not comply with the covenants or otherwise default under them, we may not have the funds necessary to pay all amounts that could become due and the lenders could foreclose on substantially all of our assets.***

Our indebtedness contains covenants that, among other things, significantly restricts and, in some cases, effectively eliminates our ability and the ability of our subsidiaries to:

incur additional debt;

create or incur liens;

bid on or perform work due to limits on the amount of performance bonds that may be secured by letters of credit;

pay dividends or make other equity distributions to our stockholders;

make investments;

sell assets;

issue or become liable on a guarantee;

create or acquire new subsidiaries;

effect a merger or consolidation of, or sell all or substantially all of our assets; and

raise capital using our equity.

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In addition, we must comply with certain financial covenants. In the event we were to fail to meet any of such covenants and were unable to cure such breach or otherwise renegotiate such covenants, our lenders would have significant rights to deny future access to liquidity and/or seize control of substantially all of our assets. The material financial covenants with which we must comply include a maximum first lien leverage ratio, a maximum total leverage ratio, a minimum liquidity ratio, a minimum fixed charge coverage ratio, and a minimum consolidated EBITDA.

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The covenants contained in our indebtedness and any credit agreement governing future debt may significantly restrict our future operations. Furthermore, upon the occurrence of any event of default, our lenders could elect to declare all amounts outstanding under such agreements, together with accrued interest, to be immediately due and payable. If those lenders were to accelerate the payment of those amounts, we may not have sufficient assets to repay those amounts in full.

On June 4, 2009, we filed a complaint in the United States District Court for the Northern District of Ohio against the lenders under our credit agreement, Field Point III, Ltd. and SPF CDO I, Ltd., both affiliates of Silverpoint, and KeyBank National Association seeking equitable relief in the form of reformation of an error in a contract schedule, declaratory relief and damages. The error resulted from the erroneous preparation of a schedule to the loan documents consisting of calculations relating to a financial covenant. We are specifically seeking reformation of the error in the Minimum Liquidity Ratio covenant. KeyBank has agreed to reform the error; however, any reformation requires Silverpoint's consent, which has not been provided. To date, we have met this covenant without the requested reformation. However, because the magnitude of the error in the schedule increases in future periods, we believe that it will become more challenging to continue to manage around the error in the Minimum Liquidity Ratio covenant unless the error is corrected or we take alternative actions.

On August 27, 2009, we entered into a term sheet, which was negotiated under the jurisdiction of the United States District Court for the Northern District of Ohio, under which the parties intend to settle this dispute. The term sheet provides that a definitive settlement agreement will be negotiated and executed on or before September 27, 2009 and, if executed, would effect the reformation of the minimum liquidity ratio in accordance with our request. The term sheet also requires that we use the net proceeds from the sale of the securities under this prospectus supplement to pay down the first term loan at par with no prepayment penalty or make whole payments. The term sheet also provides that we will agree to pay a fee of \$500,000 to our lenders in connection with the execution of a definitive settlement agreement and that the lenders will extend the term of the revolving line of credit by one year to December 31, 2012. In addition, the term sheet provides, among other things, that the parties will execute and deliver mutual releases. The amendments described in this paragraph will not be effective unless and until the parties have executed a definitive settlement agreement, and we can provide no assurance that the definitive settlement agreement will be entered into on the anticipated terms, or at all.

We are also subject to interest rate risk due to our indebtedness at variable interest rates, based on a base rate or LIBOR floor rate plus an applicable margin. Shifts in interest rates could have a material adverse effect on us.

*We may be required to prepay our indebtedness prior to its stated maturity, which may limit our ability to pursue business opportunities.*

Pursuant to the terms of certain of our indebtedness, in certain instances we are required to prepay outstanding indebtedness prior to its stated maturity date. Specifically, certain non-recurring cash inflows such as proceeds from asset sales, insurance recoveries, and equity offerings may have to be used to pay down indebtedness and may not be reborrowed. These prepayment provisions may limit our ability to utilize this cash flow to pursue business opportunities.

**Risks Related to Investments in our Securities**

*We may allocate the net proceeds from this offering in ways that you and other stockholders may not approve.*

We intend to use the net proceeds from this offering to repay existing indebtedness. To the extent that the net proceeds are not applied to repay existing indebtedness, we intend to use them for general corporate purposes, including the acquisition or investment in businesses, services and technologies that are complementary to our own and other general corporate expenses. In general, our management will have broad discretion in the application of the net proceeds from this offering and could spend the

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proceeds in ways that do not necessarily improve our operating results or enhance the value of our common stock.

***The price of our common stock may fluctuate significantly and you may not be able to resell your shares at or above the price you pay for them.***

The stock market in general and the stock prices of government services companies in particular, have experienced volatility that has often been unrelated to or disproportionate to the operating performance of those companies. The market price of our common stock has fluctuated in the past and is likely to fluctuate in the future. Factors which could have a significant impact on the market price of our common stock include, but are not limited to, the following:

quarterly variations in operating results;

announcements of new services by us or our competitors;

the gain or loss of significant customers;

changes in analysts' earnings estimates;

rumors or dissemination of false information;

pricing pressures;

short selling of our common stock;

impact of litigation and ongoing government inquiries;

general conditions in the market;

political and/or military events associated with current worldwide conflicts; and

events affecting other companies that investors deem comparable to us.

Companies that have experienced volatility in the market price of their stock have frequently been the subject of securities class action litigation. We and certain of our current and former officers and directors have been named defendants in class action and derivative lawsuits. These matters and any other securities class action litigation and derivative lawsuits in which we may be involved could result in substantial costs to us and a diversion of our management's attention and resources, which could materially harm our financial condition and results of operations.

***Our charter documents and Delaware law may deter potential acquirers and may depress our stock price.***

Certain provisions of our charter documents and Delaware law, as well as certain agreements we have with our executives, could make it substantially more difficult for a third party to acquire control of us. These provisions include:

authorizing the board of directors to issue preferred stock;

prohibiting cumulative voting in the election of directors;

prohibiting stockholder action by written consent;

establishing advance notice requirements for nominations for election to our board of directors or for proposing matters that can be acted on by stockholders at meetings of our stockholders;

Section 203 of the Delaware General Corporation Law, which prohibits us from engaging in a business combination with an interested stockholder unless specific conditions are met; and

a number of our executives have agreements with us that entitle them to payments in certain circumstances following a change in control.

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We have a stockholder rights plan which may discourage certain types of transactions involving an actual or potential change in control and may limit our stockholders' ability to approve transactions that they deem to be in their best interests. As a result, these provisions may depress our stock price.

*We have never paid dividends on our capital stock, and we do not anticipate paying any cash dividends in the foreseeable future.*

We have paid no cash dividends on any of our classes of capital stock to date and we currently intend to retain our future earnings, if any, to fund the development and growth of our business. We do not anticipate paying any cash dividends on our common stock in the foreseeable future. Furthermore, our credit facility restricts our ability to pay dividends. As a result, capital appreciation, if any, of our common stock will be your sole source of gain for the foreseeable future.

**CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS**

This prospectus supplement, the accompanying prospectus and the documents incorporated by reference herein and therein contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934 (the "Exchange Act"). These statements involve known and unknown risks, uncertainties and other important factors that may cause our actual results, performance or achievements to be materially different from any future results, performances or achievements expressed or implied by the forward-looking statements. Forward-looking statements may include, but are not limited to, statements relating to our future financial performance, the growth of the market for our services, expansion plans and opportunities and statements regarding our intended uses of the proceeds of the securities offered hereby. In some cases, you can identify forward-looking statements by terminology such as "may," "will," "should," "expect," "plan," "anticipate," "believe," "estimate," "predict," "potential" or "continue," the negative of such terms or other comparable terminology.

Forward-looking statements reflect our current views with respect to future events, outlooks or expectations for earnings, revenues, expenses or other future financial or business performance, strategies or expectations or the impact of legal or regulatory matters on business, results of operations or financial conditions, are based on assumptions and are subject to risks, uncertainties and other important factors. Risk factors that could cause actual results to differ from those contained in the forward-looking statements include but are not limited to: changes in the scope or timing of our projects; changes or cutbacks in spending or the appropriation of funding by the federal government, including the U.S. Department of Defense, which could cause delays or cancellations of key government contracts; the timing, rescheduling or cancellation of significant customer contracts and agreements, or consolidation by or the loss of key customers; risks of adverse regulatory action or litigation; risks associated with debt leverage; failure to obtain court approval of the proposed litigation settlement or to ultimately settle the litigation; failure to successfully consummate acquisitions or integrate acquired operations; competition in the marketplace which could reduce revenues and profit margins; and other important factors that we discuss in greater detail under the heading "Risk Factors" contained in this prospectus supplement and any related free writing prospectus, and in our most recent annual report on Form 10-K and in our quarterly reports on Form 10-Q for the periods ended March 29, 2009 and June 28, 2009, as well as any amendments thereto reflected in subsequent filings with the SEC. Given these risks, uncertainties and other important factors, you should not place undue reliance on these forward-looking statements. You should carefully read this prospectus supplement, the accompanying prospectus and any related free writing prospectus, together with the information incorporated herein by reference as described under the headings "Where You Can Find Additional Information" and "Incorporation of Certain Documents by Reference," completely and with the understanding that our actual future results may be materially different from what we expect.

These forward-looking statements represent our estimates and assumptions only as of the date such forward-looking statements are made. Except as required by law, we assume no obligation to update any forward-looking statements publicly, or to update the reasons actual results could differ materially from those anticipated in any forward-looking statements, even if new information becomes available in the future.

Table of Contents**USE OF PROCEEDS**

We expect the net proceeds from this offering to be up to approximately \$17.6 million after deducting placement agent fees, as described in "Plan of Distribution," and other estimated offering expenses payable by us, which include legal, accounting and printing fees. We intend to use the net proceeds from the sale of the securities under this prospectus supplement to repay existing indebtedness. To the extent that the net proceeds are not applied to repay existing indebtedness, we intend to use them for the acquisition or investment in businesses, services and technologies that are complementary to our own and other general corporate expenses.

The credit facility provides for two term loans consisting of a first lien term note and a second lien term note, as well as a first lien revolving line of credit. The first lien term loan has a five year term with principal payments of \$0.6 million required quarterly beginning on March 31, 2008, \$1.3 million in 2009, \$2.5 million in 2010, and \$4.1 million in 2011 and 2012. The revolving line of credit has a four year term which expires on December 31, 2011. As of June 28, 2009, our outstanding balance on the credit facility was \$75.2 million and the weighted average interest rate was 10.53%.

As of the date of this prospectus supplement, we cannot specify with certainty all of the particular uses of the proceeds from this offering. Accordingly, we will retain broad discretion over the use of such proceeds. Pending the use of the net proceeds from this offering as described above, we intend to invest the net proceeds in short-term, investment-grade securities.

**DILUTION**

Our net tangible book deficit on June 28, 2009 was approximately 36.6 million, or approximately \$(0.28) per share of common stock. Net tangible book value (deficit) per share is determined by dividing our net tangible book value (deficit), which consists of tangible assets less total liabilities, by the number of shares of common stock outstanding on that date. Without taking into account any other changes in the net tangible book value after June 28, 2009, other than to give effect to our receipt of the estimated net proceeds from the sale of 26.0 million shares of common stock at an offering price of \$0.72 per share, less the placement agent fees and our estimated offering expenses, our net tangible book deficit as of June 28, 2009, after giving effect to the items above, would have been approximately \$19.0 million, or \$(0.12) per share. This represents an immediate decrease in the net tangible book deficit of \$0.16 per share to existing stockholders and an immediate dilution of \$0.84 per share to new investors. The following table illustrates this per share dilution:

Offering price per share of common stock	\$ 0.72
Net tangible book deficit per share as of June 28, 2009	\$(0.28)
Decrease in net tangible book deficit per share attributable to the offering	\$ 0.16
Pro forma net tangible book deficit per share as of June 28, 2009, after giving effect to the offering	\$(0.12)
Dilution per share to new investors in the offering	\$ 0.84

The above table is based on 129,882,339 shares of common stock outstanding as of June 28, 2009, and excludes, as of that date:

14,756,102 shares of common stock issuable upon the exercise of outstanding stock options with a weighted average exercise price of \$2.86 per share;

10,635,596 shares of common stock available for future grant under our 1999 Equity Incentive Plan, 2000 Non-Statutory Stock Option Plan and 2005 Equity Incentive Plan (the "Equity Incentive Plans");

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4,430,792 shares of common stock issuable upon the vesting and settlement of restricted stock units;

approximately 1,610,916 shares of common stock which may be issued upon conversion of outstanding subordinated convertible promissory notes and warrants; and

1,000,000 shares of common stock which may be issued upon conversion of 10,000 shares of Series B Preferred Shares.

To the extent that any of these options are exercised, restricted stock units are settled, new options or restricted stock units are issued under our Equity Incentive Plans or we issue additional shares of common stock in the future, there will be further dilution to new investors.

**PLAN OF DISTRIBUTION**

B. Riley & Co., LLC, which we refer to as the placement agent, has agreed to act as the exclusive placement agent in connection with this offering subject to the terms and conditions of a placement agent agreement, dated August 27, 2009. The placement agent is not required to arrange the purchase or sale of any specific number or dollar amount of common stock, but has agreed to use its reasonable best efforts to arrange for the sale of all of the common stock offered hereby. Therefore, we may not sell the entire amount of shares offered pursuant to this prospectus supplement. The placement agent proposes to arrange for the sale to one or more purchasers of the common stock offered pursuant to this prospectus supplement. B. Riley & Co., LLC intends, but is not obligated, to purchase up to approximately 4,000,000 shares of the common stock sold in this offering. We have agreed to pay the placement agent an aggregate placement agent's fee equal to five percent of the gross proceeds in this offering.

The following table shows the per share and total placement agent's fee we will pay to the placement agent in connection with the sale of the common stock offered pursuant to this prospectus supplement assuming the purchase of all of the shares of common stock offered hereby:

Per share	\$ 0.036
Total	\$936,000

Because there is no minimum offering amount required as a condition to closing in this offering, the actual total offering commissions, if any, are not presently determinable and may be substantially less than the maximum amount set forth above. The maximum commission or discount to be received by any member of the Financial Industry Regulatory Association, or FINRA, or independent broker-dealer may not be greater than eight percent of the initial gross proceeds from the sale of any shares of common stock being offered hereby. We have also agreed to reimburse the placement agent for certain reasonable travel, legal and other out-of-pocket expenses.

We currently anticipate that the sale of 26,000,000 shares of common stock will be completed on or about September 2, 2009. We estimate the total offering expenses of this offering that will be payable by us, excluding the placement agent's fee, will be approximately \$160,000, which include legal and printing costs, various other fees and reimbursement of the placements agent's expenses. At the closing, The Depository Trust Company will credit the shares of common stock to the respective accounts of the investors.

We have agreed to indemnify the placement agent against liabilities under the Securities Act of 1933, as amended. We have also agreed to contribute to payments the placement agent may be required to make in respect of such liabilities.

We, along with certain of our executive officers, have agreed to certain lock-up provisions with regard to future sales of our common stock and other securities exercisable or exchangeable for

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common stock for a period of 180 days with respect to us and a 90 day period with respect to such executive officers.

The foregoing does not purport to be a complete statement of the terms and conditions of the placement agent agreement. A copy of the placement agent agreement is included as an exhibit to our current report on Form 8-K that will be filed with the SEC and incorporated by reference into the Registration Statement of which this prospectus supplement forms a part. See "Where You Can Find More Information" on page S-24 and "Incorporation of Certain Documents by Reference" on page S-25.

The placement agent may be deemed to be an underwriter within the meaning of Section 2(a)(11) of the Securities Act, and any commissions received by it and any profit realized on the resale of the units sold by it while acting as principal might be deemed to be underwriting discounts or commissions under the Securities Act. As underwriter, the placement agent would be required to comply with the requirements of the Securities Act and the Securities Exchange Act of 1934, as amended, including, without limitation, Rule 415(a)(4) under the Securities Act and Rule 10b-5 and Regulation M under the Exchange Act. These rules and regulations may limit the timing of purchases and sales of shares of common stock by the placement agent acting as principal. Under these rules and regulations, the placement agent:

must not engage in any stabilization activity in connection with our securities; and

must not bid for or purchase any of our securities or attempt to induce any person to purchase any of our securities, other than as permitted under the Exchange Act, until they have completed their participation in the distribution.

#### **LEGAL MATTERS**

The validity of the securities being offered by this prospectus will be passed upon by our counsel, Morrison & Foerster LLP, San Diego, California. The placement agent is being represented in connection with this offering by Paul, Hastings, Janofsky & Walker LLP, Los Angeles, California.

#### **EXPERTS**

Grant Thornton LLP, independent registered public accounting firm, has audited our consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 28, 2008 as set forth in their report, which is incorporated by reference in this prospectus and elsewhere in the registration statement. Our consolidated financial statements are incorporated by reference in reliance on Grant Thornton LLP's reports, given on its authority as experts in accounting and auditing.

#### **WHERE YOU CAN FIND ADDITIONAL INFORMATION**

We file annual, quarterly and special reports, proxy statements and other information with the SEC. You may read and copy any document we file at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for more information about the operation of the public reference room. The SEC maintains an internet website that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, including Kratos Defense & Security Solutions, Inc. You may also access our reports and proxy statements free of charge at our website, <http://www.kratosdefense.com>. The information contained in, or that can be accessed through, our website is not part of this prospectus supplement. The prospectus included in this filing is part of a registration statement filed by us with the SEC. The full registration statement can be obtained from the SEC, as indicated above, or from us.

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**INCORPORATION OF CERTAIN DOCUMENTS BY REFERENCE**

The SEC allows us to incorporate by reference the information we file with it, which means that we can disclose important information to you by referring you to another document that we have filed separately with the SEC. We hereby incorporate by reference the following information or documents into this prospectus supplement and the accompanying prospectus:

our Annual Report on Form 10-K for the fiscal year ended December 28, 2008 filed with the SEC on March 10, 2009;

our Quarterly Report on Form 10-Q for the fiscal quarter ended March 29, 2009 filed with the SEC on May 12, 2009;

our Quarterly Report on Form 10-Q for the fiscal quarter ended June 28, 2009 filed with the SEC on August 6, 2009

our Definitive Proxy Statement on Schedule 14A filed with the SEC on April 27, 2009;

our Current Reports on Form 8-K filed with the SEC on December 31, 2008, January 23, 2009, February 13, 2009, June 10, 2009, August 6, 2009 (with respect to Item 3.03 only), August 13, 2009 and August 28, 2009;

the description of our Common Stock contained in our Registration Statement on Form 8-A (File No. 000-27231), filed under Section 12(g) of the Exchange Act on September 3, 1999, including any subsequent amendment or report filed for the purpose of amending such description; and

the description of the purchase rights for Series C Preferred Stock, par value \$0.001 per share, contained in our Registration Statement on Form 8-A (File No. 000-27231), initially filed under Section 12(g) of the Exchange Act on December 17, 2004, including any subsequent amendment or report filed for the purpose of amending such description.

Any information in any of the foregoing documents will automatically be deemed to be modified or superseded to the extent that information in this prospectus supplement or accompanying prospectus or in a later filed document that is incorporated or deemed to be incorporated herein by reference modifies or replaces such information.

We also incorporate by reference any future filings (other than current reports furnished under Item 2.02 or Item 7.01 of Form 8-K and exhibits filed on such form that are related to such items) made with the SEC pursuant to Sections 13(a), 13(c), 14 or 15(d) of the Exchange Act, until we file a post-effective amendment that indicates the termination of the offering of the securities made by this prospectus. Information in such future filings updates and supplements the information provided in this prospectus. Any statements in any such future filings will automatically be deemed to modify and supersede any information in any document we previously filed with the SEC that is incorporated or deemed to be incorporated herein by reference to the extent that statements in the later filed document modify or replace such earlier statements.

Upon written or oral request, we will provide you without charge a copy of any or all of the documents that are incorporated by reference into this prospectus supplement and the accompanying prospectus but not delivered with the prospectus, including exhibits which are specifically incorporated by reference into such documents. Requests should be directed to: Kratos Defense & Security Solutions, Inc., Attention: Investor Relations, 4810 Eastgate Mall, San Diego, California, 92121, telephone (858) 812-7300.

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**PROSPECTUS**

**\$100,000,000  
Common Stock  
Preferred Stock  
Debt Securities  
Warrants  
Units**

From time to time, we may offer up to \$100,000,000 of any combination of the securities described in this prospectus, either individually or in units. We may also offer common stock or preferred stock upon conversion of debt securities, common stock upon conversion of preferred stock, or common stock, preferred stock or debt securities upon the exercise of warrants.

We will provide the specific terms of these offerings and securities in one or more supplements to this prospectus. We may also authorize one or more free writing prospectuses to be provided to you in connection with these offerings. The prospectus supplement and any related free writing prospectus may also add, update or change information contained in this prospectus. You should carefully read this prospectus, the applicable prospectus supplement and any related free writing prospectus, as well as any documents incorporated by reference, before buying any of the securities being offered.

Our common stock is traded on the Nasdaq Global Select Market under the symbol "KTOS." On August 12, 2009, the last reported sale price of our common stock on the Nasdaq Global Select Market was \$0.84. The applicable prospectus supplement will contain information, where applicable, as to any other listing, if any, on the Nasdaq Global Select Market or any securities market or other exchange of the securities covered by the applicable prospectus supplement.

**Investing in our securities involves a high degree of risk. You should review carefully the risks and uncertainties described under the heading "Risk Factors" contained in the applicable prospectus supplement and any related free writing prospectus, and under similar headings in the other documents that are incorporated by reference into this prospectus.**

**This prospectus may not be used to consummate a sale of any securities unless accompanied by a prospectus supplement.**

The securities may be sold directly by us to investors, through agents designated from time to time or to or through underwriters or dealers, on a continuous or delayed basis. For additional information on the methods of sale, you should refer to the section entitled "Plan of Distribution" in this prospectus. If any agents or underwriters are involved in the sale of any securities with respect to which this prospectus is being delivered, the names of such agents or underwriters and any applicable fees, commissions, discounts and over-allotment options will be set forth in a prospectus supplement. The price to the public of such securities and the net proceeds that we expect to receive from such sale will also be set forth in a prospectus supplement.

**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.**

The date of this prospectus is August 21, 2009.

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**ABOUT THIS PROSPECTUS**

This prospectus is part of a registration statement on Form S-3 that we filed with the Securities and Exchange Commission utilizing a "shelf" registration process. Under this shelf registration process, we may offer shares of our common stock and preferred stock, various series of debt securities and/or warrants to purchase any of such securities, either individually or in units, in one or more offerings, up to a total dollar amount of \$100,000,000. This prospectus provides you with a general description of the securities we may offer. Each time we offer a type or series of securities under this prospectus, we will provide a prospectus supplement that will contain more specific information about the terms of those securities. We may also authorize one or more free writing prospectuses to be provided to you that may contain material information relating to these offerings. We may also add or update in the prospectus supplement (and in any related free writing prospectus that we may authorize to be provided to you) any of the information contained in this prospectus or in the documents that we have incorporated by reference into this prospectus. We urge you to carefully read this prospectus, any applicable prospectus supplement and any related free writing prospectus, together with the information incorporated herein by reference as described under the heading "Where You Can Find Additional Information," before buying any of the securities being offered. **THIS PROSPECTUS MAY NOT BE USED TO CONSUMMATE A SALE OF SECURITIES UNLESS IT IS ACCOMPANIED BY A PROSPECTUS SUPPLEMENT.**

You should rely only on the information that we have provided or incorporated by reference in this prospectus, any applicable prospectus supplement and any related free writing prospectus that we may authorize to be provided to you. We have not authorized anyone to provide you with different information. No dealer, salesperson or other person is authorized to give any information or to represent anything not contained in this prospectus, any applicable prospectus supplement or any related free writing prospectus that we may authorize to be provided to you. You must not rely on any unauthorized information or representation. This prospectus is an offer to sell only the securities offered hereby, but only under circumstances and in jurisdictions where it is lawful to do so. You should assume that the information in this prospectus, any applicable prospectus supplement or any related free writing prospectus is accurate only as of the date on the front of the document and that any information we have incorporated by reference is accurate only as of the date of the document incorporated by reference, regardless of the time of delivery of this prospectus, any applicable prospectus supplement or any related free writing prospectus, or any sale of a security.

This prospectus contains summaries of certain provisions contained in some of the documents described herein, but reference is made to the actual documents for complete information. All of the summaries are qualified in their entirety by the actual documents. Copies of some of the documents referred to herein have been filed, will be filed or will be incorporated by reference as exhibits to the registration statement of which this prospectus is a part, and you may obtain copies of those documents as described below under the heading "Where You Can Find Additional Information."

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**KRATOS DEFENSE & SECURITY SOLUTIONS, INC.**

Kratos Defense & Security Solutions, Inc. is an innovative provider of mission critical engineering, information technology services and warfighter solutions. We work primarily for the U.S. government and federal government agencies, but we also perform work for state and local agencies and commercial customers. Our principal services are related to, but are not limited to, Command, Control, Communications, Computing, Intelligence, Surveillance and Reconnaissance (C4ISR); weapons systems lifecycle support and sustainment; military weapon range operations and technical services; missile, rocket and weapons system test and evaluation; missile and rocket mission launch services; public safety, security and surveillance systems; modeling and simulation; unmanned aerial vehicle products and technology; advanced network engineering and information technology services; and advanced information technology services. We offer our customers solutions and expertise to support their mission-critical needs by leveraging our skills across our core service areas.

We derive a substantial portion of our revenue from contracts performed for federal government agencies, including the U.S. Department of Defense (DOD), with the majority of our revenue currently generated from the delivery of mission-critical warfighter solutions, advanced engineering services, system integration and system sustainment services to defense and other non-DOD and civilian government agencies. We believe our diversified and stable client base, strong client relationships, broad array of contract vehicles, considerable employee base possessing government security clearances, extensive list of past performance qualifications, and significant management and operational capabilities position us for continued growth.

Prior to 2008 we were also an independent provider of outsourced engineering and network deployment services, security systems engineering and integration services and other technical services for the wireless communications industry, the U.S. government and enterprise customers. In 2006 and 2007, we undertook a transformation strategy whereby we divested our commercial wireless-related businesses and chose to pursue business with the federal government, primarily the DOD, through strategic acquisitions. On September 12, 2007, we changed our name from Wireless Facilities, Inc. to Kratos Defense & Security Solutions, Inc. In connection with our name change, we changed our NASDAQ Global Market trading symbol to "KTOS".

Our executive offices are located at 4810 Eastgate Mall, San Diego, California 92121, and our telephone number is (858) 812-7300. We maintain an Internet website at [www.kratosdefense.com](http://www.kratosdefense.com). Information contained in or accessible through our website does not constitute part of this prospectus.

Unless otherwise mentioned or unless the context requires otherwise, all references in this prospectus to "we," "us," "our" and "Kratos" refer to Kratos Defense & Security Solutions, Inc., a Delaware corporation.

**RISK FACTORS**

Investing in our securities involves a high degree of risk. You should carefully review the risks and uncertainties described under the heading "Risk Factors" contained in the applicable prospectus supplement and any related free writing prospectus, and under similar headings in the other documents, including our most recent annual report on Form 10-K, any subsequent quarterly reports on Form 10-Q or current report on Form 8-K we file after the date of this prospectus, that are incorporated by reference into this prospectus. The occurrence of any of these risks might cause you to lose all or part of your investment in the offered securities. Additional risks not presently known to us or that we currently believe are immaterial may also significantly impair our business operations and financial condition.

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**CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS**

This prospectus and the documents incorporated by reference contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934 (the "Exchange Act"). These statements involve known and unknown risks, uncertainties and other important factors that may cause our actual results, performance or achievements to be materially different from any future results, performances or achievements expressed or implied by the forward-looking statements. Forward-looking statements may include statements relating to:

our future financial performance;

the growth of the market for our products and services;

expansion plans and opportunities; and

consolidation in the market or industries for our products and services.

In some cases, you can identify forward-looking statements by terminology such as "may," "will," "should," "expect," "plan," "anticipate," "believe," "estimate," "predict," "potential" or "continue," the negative of such terms or other comparable terminology.

Forward-looking statements reflect our current views with respect to future events, outlooks or expectations for earnings, revenues, expenses or other future financial or business performance, strategies or expectations or the impact of legal or regulatory matters on business, results of operations or financial conditions, are based on assumptions and are subject to risks, uncertainties and other important factors. Risk factors that could cause actual results to differ from those contained in the forward-looking statements include but are not limited to: changes in the scope or timing of our projects; changes or cutbacks in spending or the appropriation of funding by the federal government, including the DOD, which could cause delays or cancellations of key government contracts; the timing, rescheduling or cancellation of significant customer contracts and agreements, or consolidation by or the loss of key customers; risks of adverse regulatory action or litigation; risks associated with debt leverage; failure to obtain court approval of the proposed litigation settlement or to ultimately settle the litigation; failure to successfully consummate acquisitions or integrate acquired operations; competition in the marketplace which could reduce revenues and profit margins; and other important factors that we discuss in greater detail under the heading "Risk Factors" contained in the applicable prospectus supplement and any related free writing prospectus, and in our most recent annual report on Form 10-K and in our most recent quarterly report on Form 10-Q, as well as any amendments thereto reflected in subsequent filings with the SEC. Given these risks, uncertainties and other important factors, you should not place undue reliance on these forward-looking statements. You should carefully read both this prospectus, the applicable prospectus supplement and any related free writing prospectus, together with the information incorporated herein by reference as described under the heading "Where You Can Find Additional Information," completely and with the understanding that our actual future results may be materially different from what we expect.

These forward-looking statements represent our estimates and assumptions only as of the date such forward-looking statements are made. Except as required by law, we assume no obligation to update any forward-looking statements publicly, or to update the reasons actual results could differ materially from those anticipated in any forward-looking statements, even if new information becomes available in the future.

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**THE SECURITIES WE MAY OFFER**

We may offer shares of our common stock and preferred stock, various series of debt securities and/or warrants to purchase any of such securities, either individually or in units, with a total value of up to \$100,000,000 from time to time under this prospectus at prices and on terms to be determined by market conditions at the time of any offering. This prospectus provides you with a general description of the securities we may offer. Each time we offer a type or series of securities under this prospectus, we will provide a prospectus supplement that will describe the specific amounts, prices and other important terms of the securities, including, to the extent applicable:

designation or classification;

aggregate principal amount or aggregate offering price;

maturity, if applicable;

original issue discount, if any;

rates and times of payment of interest or dividends, if any;

redemption, conversion, exercise, exchange or sinking fund terms, if any;

ranking;

restrictive covenants, if any;

voting or other rights, if any;

conversion prices, if any; and

important United States federal income tax considerations.

The prospectus supplement and any related free writing prospectus that we may authorize to be provided to you may also add or update information contained in this prospectus or in documents we have incorporated by reference. However, no prospectus supplement or free writing prospectus will offer a security that is not registered and described in this prospectus at the time of the effectiveness of the registration statement of which this prospectus is a part.

**THIS PROSPECTUS MAY NOT BE USED TO CONSUMMATE A SALE OF SECURITIES UNLESS IT IS ACCOMPANIED BY A PROSPECTUS SUPPLEMENT.**

We may sell the securities directly to investors or to or through agents, underwriters or dealers. We, and our agents or underwriters, reserve the right to accept or reject all or part of any proposed purchase of securities. If we do offer securities to or through agents or underwriters, we will include in the applicable prospectus supplement:

the names of those agents or underwriters;

applicable fees, discounts and commissions to be paid to them;

details regarding over-allotment options, if any; and

the net proceeds to us.

*Common Stock.* We may issue shares of our common stock from time to time. The holders of common stock are entitled to one vote for each share held of record on all matters submitted to a vote of stockholders and do not have cumulative voting rights. Subject to preferences that may be applicable to any outstanding shares of preferred stock, the holders of common stock are entitled to receive ratably only those dividends as may be declared by our board of directors out of legally available funds. Upon our liquidation, dissolution or winding up, holders of our common stock are entitled to share

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ratably in all assets remaining after payment of liabilities and the liquidation preferences of any outstanding shares of preferred stock.

*Preferred Stock.* We may issue shares of our preferred stock from time to time, in one or more series. Under our amended and restated certificate of incorporation, our board of directors has the authority, without further action by stockholders, to designate up to 5,000,000 shares of preferred stock in one or more series and to fix the rights, preferences, privileges, qualifications and restrictions granted to or imposed upon the preferred stock, including dividend rights, conversion rights, voting rights, rights and terms of redemption, liquidation preference and sinking fund terms, any or all of which may be greater than the rights of the common stock.

If we sell any series of preferred stock under this prospectus, we will fix the designations, powers, preferences and rights of such series of preferred stock, as well as the qualifications, limitations or restrictions thereon, in the certificate of designation relating to that series. We will file as an exhibit to the registration statement of which this prospectus is a part, or will incorporate by reference from reports that we file with the SEC, the form of any certificate of designation that describes the terms of the series of preferred stock we are offering before the issuance of the related series of preferred stock. We urge you to read the applicable prospectus supplement (and any free writing prospectus that we may authorize to be provided to you) related to the series of preferred stock being offered, as well as the complete certificate of designation that contains the terms of the applicable series of preferred stock.

*Debt Securities.* We may issue debt securities from time to time, in one or more series, as either senior or subordinated debt or as senior or subordinated convertible debt. The senior debt securities will rank equally with any other unsecured and unsubordinated debt. The subordinated debt securities will be subordinate and junior in right of payment, to the extent and in the manner described in the instrument governing the debt, to all of our senior indebtedness. Convertible debt securities will be convertible into or exchangeable for our common stock or our other securities. Conversion may be mandatory or at your option and would be at prescribed conversion rates.

The debt securities will be issued under one or more indentures, which are contracts between us and a national banking association or other eligible party, as trustee. In this prospectus, we have summarized certain general features of the debt securities. We urge you, however, to read the applicable prospectus supplement (and any free writing prospectus that we may authorize to be provided to you) related to the series of debt securities being offered, as well as the complete indentures that contain the terms of the debt securities. Forms of indentures have been filed as exhibits to the registration statement of which this prospectus is a part, and supplemental indentures and forms of debt securities containing the terms of the debt securities being offered will be filed as exhibits to the registration statement of which this prospectus is a part or will be incorporated by reference from reports that we file with the SEC.

*Warrants.* We may issue warrants for the purchase of common stock, preferred stock and/or debt securities in one or more series. We may issue warrants independently or together with common stock, preferred stock and/or debt securities, and the warrants may be attached to or separate from these securities. In this prospectus, we have summarized certain general features of the warrants. We urge you, however, to read the applicable prospectus supplement (and any free writing prospectus that we may authorize to be provided to you) related to the particular series of warrants being offered, as well as the complete warrant agreements and warrant certificates that contain the terms of the warrants. We will file as an exhibit to the registration statement of which this prospectus is a part, or will incorporate by reference from reports that we file with the SEC, forms of the warrant agreements and forms of warrant certificates containing the terms of the warrants being offered.

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We will evidence each series of warrants by warrant certificates that we will issue. Warrants may be issued under an applicable warrant agreement that we enter into with a warrant agent. We will indicate the name and address of the warrant agent, if applicable, in the prospectus supplement relating to the particular series of warrants being offered.

*Units.* We may issue, in one or more series, units consisting of common stock, preferred stock, debt securities and/or warrants for the purchase of common stock, preferred stock and/or debt securities in any combination. In this prospectus, we have summarized certain general features of the units. We urge you, however, to read the applicable prospectus supplement (and any free writing prospectus that we may authorize to be provided to you) related to the series of units being offered, as well as the complete unit agreement that contains the terms of the units. We will file as exhibits to the registration statement of which this prospectus is a part, or will incorporate by reference from reports that we file with the SEC, the form of unit agreement and any supplemental agreements that describe the terms of the series of units we are offering before the issuance of the related series of units.

We will evidence each series of units by unit certificates that we will issue. Units may be issued under a unit agreement that we enter into with a unit agent. We will indicate the name and address of the unit agent, if applicable, in the prospectus supplement relating to the particular series of units being offered.

**RATIO OF EARNINGS TO FIXED CHARGES**

The following summary is qualified by the more detailed information appearing in the computation table found in Exhibit 12.1 to the registration statement of which this prospectus is part and the historical financial statements, including the notes to those financial statements, incorporated by reference in this prospectus.

Our earnings are inadequate to cover fixed charges. The following table sets forth the dollar amount of the coverage deficiency for all periods. We have not included a ratio of earnings to combined fixed charges and preferred stock dividends because no preferred dividends are accrued, accruing or payable on our outstanding preference shares.

	<b>Six Months Ended June 28, 2009</b>	<b>12/28/2008</b>	<b>12/31/2007</b>	<b>Year Ended</b>		
				<b>12/31/2006</b>	<b>12/31/2005</b>	<b>12/31/2004</b>
Ratio of Earnings to Fixed Charges						
Deficiency of Earnings Available to Cover Fixed Charges	\$ (40.6)	\$ (104.7)	\$ (25.9)	\$ (26.7)	\$ (0.6)	\$ (19.7)

**USE OF PROCEEDS**

Except as described in any prospectus supplement or in any related free writing prospectus that we may authorize to be provided to you, we currently intend to use the net proceeds from the sale of the securities offered hereby for general corporate purposes, including, among other things, working capital requirements and potential re-payment of indebtedness that may be outstanding at the time of any offering under this prospectus. We may also use a portion of the net proceeds to acquire or invest in businesses, services and technologies that are complementary to our own. Pending these uses, we expect to invest the net proceeds in short-term, investment-grade securities.

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**DESCRIPTION OF CAPITAL STOCK**

**Authorized and Outstanding Capital Stock**

Our authorized capital stock consists of 195,000,000 shares of common stock, par value \$0.001 per share, and 5,000,000 shares of preferred stock, par value \$0.001 per share, issuable in one or more series designated by Kratos' board of directors, of which 63,637 shares have been designated Series A Preferred Stock, 90,000 shares have been designated Series B Preferred Stock and 1,200,000 have been designated Series C Preferred Stock. As of August 12, 2009, there were 130,262,590 shares of common stock, no shares of Series A Preferred Stock, 10,000 shares of Series B Preferred Stock and no shares of Series C Preferred Stock outstanding.

**Common Stock**

The holders of our common stock have one vote per share. Holders of common stock are not entitled to vote cumulatively for the election of directors. Generally, all matters to be voted on by stockholders must be approved by a majority, or, in the case of election of directors, by a plurality, of the votes cast at a meeting at which a quorum is present, voting together as a single class, subject to any voting rights granted to holders of any then outstanding preferred stock. Shares of common stock are entitled to participate equally in dividends when and as dividends may be declared by our board of directors out of funds legally available for the payment of dividends. In the event of our voluntary or involuntary liquidation, dissolution or winding up, the prior rights of our creditors and the liquidation preference of any preferred stock then outstanding must first be satisfied. The holders of common stock will be entitled to share in the remaining assets on a pro rata basis. No shares of common stock are subject to redemption or have redemptive rights to purchase additional shares of common stock.

Our common stock is listed on the Nasdaq Global Select Market under the symbol "KTOS".

**Preferred Stock**

Our certificate of incorporation provides that we may issue shares of preferred stock from time to time in one or more series. Our board of directors is authorized to fix the voting rights, if any, designations, powers, preferences, qualifications, limitations and restrictions thereof, applicable to the shares of each series. The board of directors may, without stockholder approval issue preferred stock with voting and other rights that could adversely affect the voting power and other rights of the holders of the common stock and could have anti-takeover effects, including preferred stock or rights to acquire preferred stock in connection with implementing a shareholder rights plan. The ability of the board of directors to issue preferred stock without stockholder approval could have the effect of delaying, deferring or preventing a change of control or the removal of its existing management.

*Series A Preferred Stock*

There are currently no shares of Series A Preferred Stock issued and outstanding.

*Series B Preferred Stock*

On May 30, 2002, we issued an aggregate of 90,000 shares of Series B Preferred Stock, 10,000 shares of which were outstanding on August 4, 2009. Each share of Series B Preferred Stock is currently convertible into 100 shares of common stock and will automatically convert into common stock if and when our common stock trades at or above \$11.00 per share for 30 consecutive trading days after that date. Upon any voluntary or involuntary liquidation, dissolution or winding up of our affairs, before any payment is to be made to the holders of common stock, the holders of Series B Preferred Stock are entitled to receive \$500 per share plus all accumulated or accrued and unpaid dividends for such share. Holders of shares of Series B Preferred Stock are entitled to vote on all

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matters submitted to a vote of the holders of shares of common stock, including with respect to the election of members of the board of directors, on an as-converted to common stock basis.

*Series C Preferred Stock*

On December 16, 2004, in connection with the approval of our Stockholder Rights Plan, our board of directors authorized and declared a dividend of one right to purchase on one-hundredth of a share of Series C Preferred Stock for each outstanding share of common stock to stockholders of record as of the close of business December 27, 2004. Each right entitles the registered holder, subject to the terms of the Stockholder Rights Plan, to purchase one one-hundredth of a share of Series C Preferred at a purchase price of \$54.00, subject to adjustment. The rights are not exercisable until a Distribution Date occurs (as that term is defined in the Stockholder Rights Plan) and will expire at the close of business on the tenth anniversary of the Stockholder Rights Plan unless earlier redeemed or exchanged. There are currently no shares of Series C Preferred Stock issued and outstanding.

**Anti-Takeover Provisions**

The provisions of the Delaware General Corporation Law, or DGCL, our amended and restated certificate of incorporation, amended and restated bylaws and our Stockholder Rights Plan contain provisions that could discourage or make more difficult a change in control of the Company, including an acquisition of the Company by means of a tender offer, a proxy contest and removal of our incumbent officers and directors, without the support of our board of directors. A summary of these provisions follows.

*Statutory Business Combination Provision*

We are subject to Section 203 of the DGCL, which, subject to certain exceptions, prohibits a Delaware corporation from engaging in any "business combination" with an "interested stockholder" for a period of three years following the time that such stockholder became an interested stockholder, unless:

the board of directors of the corporation approves either the business combination or the transaction that resulted in the stockholder becoming an interested stockholder, prior to the time the interested stockholder attained that status;

upon the closing of the transaction that resulted in the stockholder becoming an interested stockholder, the interested stockholder owned at least 85% of the voting stock of the corporation outstanding at the time the transaction commenced, excluding for purposes of determining the number of shares outstanding those shares owned by persons who are directors and also officers and by employee stock plans in which employee participants do not have the right to determine confidentially whether shares held subject to the plan will be tendered in a tender or exchange offer; or

at or subsequent to such time, the business combination is approved by the board of directors and authorized at an annual or special meeting of stockholders, and not by written consent, by the affirmative vote of at least two-thirds of the outstanding voting stock that is not owned by the interested stockholder.

With certain exceptions, an "interested stockholder" is a person or group who or which owns 15% or more of the corporation's outstanding voting stock (including any rights to acquire stock pursuant to an option, warrant, agreement, arrangement or understanding, or upon the exercise of conversion or exchange rights, and stock with respect to which the person has voting rights only), or is an affiliate or associate of the corporation and was the owner of 15% or more of such voting stock at any time within the previous three years.

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In general, Section 203 defines a business combination to include:

any merger or consolidation involving the corporation and the interested stockholder;

any sale, transfer, pledge or other disposition of 10% or more of the assets of the corporation involving the interested stockholder;

subject to certain exceptions, any transaction that results in the issuance or transfer by the corporation of any stock of the corporation to the interested stockholder;

any transaction involving the corporation that has the effect of increasing the proportionate share of the stock or any class or series of the corporation beneficially owned by the interested stockholder; or

the receipt by the interested stockholder of the benefit of any loans, advances, guarantees, pledges or other financial benefits provided by or through the corporation.

A Delaware corporation may "opt out" of this provision with an express provision in its original certificate of incorporation or an express provision in its amended and restated certificate of incorporation or bylaws resulting from a stockholders' amendment approved by at least a majority of the outstanding voting shares. However, Kratos has not "opted out" of this provision. Section 203 could prohibit or delay mergers or other takeover or change-in-control attempts and, accordingly, may discourage attempts to acquire Kratos.

*Stockholder Rights Plan*

We have a stockholder rights plan that may discourage certain types of transactions involving an actual or potential change in control and may limit our stockholders' ability to approve transactions that they deem to be in their best interests.

*Election and Removal of Directors*

Our board of directors is elected annually by all holders of our capital stock. Directors may be removed without cause by the affirmative vote of the holders of at least a majority of the outstanding shares entitled to vote on such removal; provided however, that unless the entire board is removed, no individual director may be removed when the votes cast against such director's removal, or not consenting in writing to such removal, would be sufficient to elect that director if voted cumulatively at an election in which the same total number of votes were cast (or if such action is taken by written consent, all shares entitled to vote were voted) and the entire number of directors authorized at the time of such directors most recent election were then being elected.

*No Stockholder Action by Written Consent*

Our certificate of incorporation provides that any action required or permitted to be taken by the holders of common stock at an annual or special meeting of stockholders must be effected at a duly called meeting and may not be taken or effected by written consent of the stockholders.

*Stockholder Meetings*

Under our amended and restated bylaws, only the chairman of the board of directors, the chief executive officer or a majority of the total number of authorized directors may call a special meeting of the stockholders, and any business conducted at any special meeting will be limited to the purpose or purposes specified in the order calling for the special meeting.

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*Requirements for Advance Notification of Stockholder Nominations and Proposals*

In order for our stockholders to properly bring nominations or business before an annual meeting, they must comply with certain notice requirements as provided by our amended and restated bylaws. Typically, in order for such notices to be timely, they must be provided to us not earlier than the close of business on the 120th day prior to such annual meeting and not later than the close of business on the later of the 90th day prior to such annual meeting. For such notices to be timely in the event the annual meeting is advanced more than 30 days prior to or delayed by more than 30 days after the anniversary of the preceding year's annual meeting, notice must be provided to us not earlier than the close of business on the 120th day prior to such annual meeting and not later than the close of business on the later of the 90th day prior to such annual meeting or the 10th day following the day on which public announcement of the date of such meeting is first made.

**Amendment of Charter Provisions**

The affirmative vote of the holders of at least 66-2/3% of the voting power of all of the then-outstanding shares of our voting stock, voting together as a single class, is required to, among other things, alter, amend or repeal certain provisions of our amended and restated certificate of incorporation, including those related to the election and removal of the board of directors, amendment of our bylaws and certificate of incorporation, restrictions against stockholder actions by written consent and the indemnification of officers and directors.

Our amended and restated bylaws may only be amended (or new bylaws adopted) by the board of directors or the affirmative vote of the holders of at least 66-2/3% of the voting power of all of the then-outstanding shares of our voting stock.

**Transfer Agent and Registrar**

The transfer agent and registrar for our common stock is Wells Fargo Bank, N.A., Shareowner Services. Its address is 161 North Concord Exchange Street, South Saint Paul, MN, 55075 and its telephone number is (800) 468-9716. The transfer agent for any series of preferred stock that we may offer under this prospectus will be named and described in the prospectus supplement for that series.

**DESCRIPTION OF DEBT SECURITIES**

We may issue debt securities, in one or more series, as either senior or subordinated debt or as senior or subordinated convertible debt. While the terms we have summarized below will apply generally to any debt securities that we may offer under this prospectus, we will describe the particular terms of any debt securities that we may offer in more detail in the applicable prospectus supplement. The terms of any debt securities offered under a prospectus supplement may differ from the terms described below. Unless the context requires otherwise, whenever we refer to the indentures, we also are referring to any supplemental indentures that specify the terms of a particular series of debt securities.

We will issue the senior debt securities under the senior indenture that we will enter into with the trustee named in the senior indenture. We will issue the subordinated debt securities under the subordinated indenture that we will enter into with the trustee named in the subordinated indenture. The indentures will be qualified under the Trust Indenture Act of 1939. We use the term "debenture trustee" to refer to either the trustee under the senior indenture or the trustee under the subordinated indenture, as applicable. We have filed forms of indentures to the registration statement of which this prospectus is a part, and supplemental indentures and forms of debt securities containing the terms of the debt securities being offered will be filed as exhibits to the registration statement of which this prospectus is a part or will be incorporated by reference from reports that we file with the SEC.

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The following summaries of material provisions of the senior debt securities, the subordinated debt securities and the indentures are subject to, and qualified in their entirety by reference to, all of the provisions of the indenture applicable to a particular series of debt securities. We urge you to read the applicable prospectus supplements and any related free writing prospectuses related to the debt securities that we may offer under this prospectus, as well as the complete indentures that contains the terms of the debt securities. Except as we may otherwise indicate, the terms of the senior indenture and the subordinated indenture are identical.

**General**

We will describe in the applicable prospectus supplement the terms of the series of debt securities being offered, including:

the title;

the principal amount being offered, and if a series, the total amount authorized and the total amount outstanding;

any limit on the amount that may be issued;

whether or not we will issue the series of debt securities in global form, the terms and who the depository will be;

the maturity date;

whether and under what circumstances, if any, we will pay additional amounts on any debt securities held by a person who is not a United States person for tax purposes, and whether we can redeem the debt securities if we have to pay such additional amounts;

the annual interest rate, which may be fixed or variable, or the method for determining the rate and the date interest will begin to accrue, the dates interest will be payable and the regular record dates for interest payment dates or the method for determining such dates;

whether or not the debt securities will be secured or unsecured, and the terms of any secured debt;

the terms of the subordination of any series of subordinated debt;

the place where payments will be payable;

restrictions on transfer, sale or other assignment, if any;

our right, if any, to defer payment of interest and the maximum length of any such deferral period;

the date, if any, after which, and the price at which, we may, at our option, redeem the series of debt securities pursuant to any optional or provisional redemption provisions and the terms of those redemption provisions;

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the date, if any, on which, and the price at which we are obligated, pursuant to any mandatory sinking fund or analogous fund provisions or otherwise, to redeem, or at the holder's option to purchase, the series of debt securities and the currency or currency unit in which the debt securities are payable;

whether the indenture will restrict our ability and/or the ability of our subsidiaries to:

incur additional indebtedness;

issue additional securities;

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create liens;

pay dividends and make distributions in respect of our capital stock and the capital stock of our subsidiaries;

redeem capital stock;

place restrictions on our subsidiaries' ability to pay dividends, make distributions or transfer assets;

make investments or other restricted payments;

sell or otherwise dispose of assets;

enter into sale-leaseback transactions;

engage in transactions with stockholders and affiliates;

issue or sell stock of our subsidiaries;

effect a consolidation or merger;

whether the indenture will require us to maintain any interest coverage, fixed charge, cash flow-based, asset-based or other financial ratios;

a discussion of any material United States federal income tax considerations applicable to the debt securities;

information describing any book-entry features;

provisions for a sinking fund purchase or other analogous fund, if any;

the applicability of the provisions in the indenture on discharge;

whether the debt securities are to be offered at a price such that they will be deemed to be offered at an "original issue discount" as defined in paragraph (a) of Section 1273 of the Internal Revenue Code;

the denominations in which we will issue the series of debt securities, if other than denominations of \$1,000 and any integral multiple thereof;

the currency of payment of debt securities if other than U.S. dollars and the manner of determining the equivalent amount in U.S. dollars; and

any other specific terms, preferences, rights or limitations of, or restrictions on, the debt securities, including any additional events of default or covenants provided with respect to the debt securities, and any terms that may be required by us or advisable under applicable laws or regulations.

**Conversion or Exchange Rights**

We will set forth in the prospectus supplement the terms on which a series of debt securities may be convertible into or exchangeable for our common stock or our other securities. We will include provisions as to whether conversion or exchange is mandatory, at the option of the holder or at our option. We may include provisions pursuant to which the number of shares of our common stock or our other securities that the holders of the series of debt securities receive would be subject to adjustment.

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**Consolidation, Merger or Sale**

Unless we provide otherwise in the prospectus supplement applicable to a particular series of debt securities, the indentures will not contain any covenant that restricts our ability to merge or consolidate, or sell, convey, transfer or otherwise dispose of all or substantially all of our assets. However, any successor to or acquirer of such assets must assume all of our obligations under the indentures or the debt securities, as appropriate. If the debt securities are convertible into or exchangeable for our other securities or securities of other entities, the person with whom we consolidate or merge or to whom we sell all of our property must make provisions for the conversion of the debt securities into securities that the holders of the debt securities would have received if they had converted the debt securities before the consolidation, merger or sale.

**Events of Default Under the Indenture**

Unless we provide otherwise in the prospectus supplement applicable to a particular series of debt securities, the following are events of default under the indentures with respect to any series of debt securities that we may issue:

if we fail to pay interest when due and payable and our failure continues for 90 days and the time for payment has not been extended or deferred;

if we fail to pay the principal, premium or sinking fund payment, if any, when due and payable and the time for payment has not been extended or delayed;

if we fail to observe or perform any other covenant contained in the debt securities or the indentures, other than a covenant specifically relating to another series of debt securities, and our failure continues for 90 days after we receive notice from the debenture trustee or holders of at least 25% in aggregate principal amount of the outstanding debt securities of the applicable series; and

if specified events of bankruptcy, insolvency or reorganization occur.

If an event of default with respect to debt securities of any series occurs and is continuing, other than an event of default specified in the last bullet point above, the debenture trustee or the holders of at least 25% in aggregate principal amount of the outstanding debt securities of that series, by notice to us in writing, and to the debenture trustee if notice is given by such holders, may declare the unpaid principal of, premium, if any, and accrued interest, if any, due and payable immediately. If an event of default specified in the last bullet point above occurs with respect to us, the principal amount of and accrued interest, if any, of each issue of debt securities then outstanding shall be due and payable without any notice or other action on the part of the debenture trustee or any holder.

The holders of a majority in principal amount of the outstanding debt securities of an affected series may waive any default or event of default with respect to the series and its consequences, except defaults or events of default regarding payment of principal, premium, if any, or interest, unless we have cured the default or event of default in accordance with the indenture. Any waiver shall cure the default or event of default.

Subject to the terms of the indentures, if an event of default under an indenture shall occur and be continuing, the debenture trustee will be under no obligation to exercise any of its rights or powers under such indenture at the request or direction of any of the holders of the applicable series of debt securities, unless such holders have offered the debenture trustee reasonable indemnity. The holders of a majority in principal amount of the outstanding debt securities of any series will have the right to direct the time, method and place of conducting any proceeding for any remedy available to the

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debenture trustee, or exercising any trust or power conferred on the debenture trustee, with respect to the debt securities of that series, provided that:

the direction so given by the holder is not in conflict with any law or the applicable indenture; and

subject to its duties under the Trust Indenture Act of 1939, the debenture trustee need not take any action that might involve it in personal liability or might be unduly prejudicial to the holders not involved in the proceeding.

A holder of the debt securities of any series will have the right to institute a proceeding under the indentures or to appoint a receiver or trustee, or to seek other remedies only if:

the holder has given written notice to the debenture trustee of a continuing event of default with respect to that series;

the holders of at least 25% in aggregate principal amount of the outstanding debt securities of that series have made written request, and such holders have offered reasonable indemnity to the debenture trustee to institute the proceeding as trustee; and

the debenture trustee does not institute the proceeding, and does not receive from the holders of a majority in aggregate principal amount of the outstanding debt securities of that series other conflicting directions within 90 days after the notice, request and offer.

These limitations do not apply to a suit instituted by a holder of debt securities if we default in the payment of the principal, premium, if any, or interest on, the debt securities.

We will periodically file statements with the debenture trustee regarding our compliance with specified covenants in the indentures.

**Modification of Indenture; Waiver**

We and the debenture trustee may change an indenture without the consent of any holders with respect to specific matters:

to fix any ambiguity, defect or inconsistency in the indenture;

to comply with the provisions described above under "Description of Debt Securities Consolidation, Merger or Sale;"

to comply with any requirements of the SEC in connection with the qualification of any indenture under the Trust Indenture Act of 1939;

to add to, delete from or revise the conditions, limitations, and restrictions on the authorized amount, terms, or purposes of issue, authentication and delivery of debt securities, as set forth in the indenture;

to provide for the issuance of and establish the form and terms and conditions of the debt securities of any series as provided under "Description of Debt Securities General" to establish the form of any certifications required to be furnished pursuant to the terms of the indenture or any series of debt securities, or to add to the rights of the holders of any series of debt securities;

to evidence and provide for the acceptance of appointment hereunder by a successor trustee;

to provide for uncertificated debt securities in addition to or in place of certificated debt securities and to make all appropriate changes for such purpose;

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to add to our covenants such new covenants, restrictions, conditions or provisions for the protection of the holders, and to make the occurrence, or the occurrence and the continuance, of a default in any such additional covenants, restrictions, conditions or provisions an event of default; or

to change anything that does not materially adversely affect the interests of any holder of debt securities of any series.

In addition, under the indentures, the rights of holders of a series of debt securities may be changed by us and the debenture trustee with the written consent of the holders of at least a majority in aggregate principal amount of the outstanding debt securities of each series that is affected. However, unless we provide otherwise in the prospectus supplement applicable to a particular series of debt securities, we and the debenture trustee may make the following changes only with the consent of each holder of any outstanding debt securities affected:

extending the fixed maturity of the series of debt securities;

reducing the principal amount, reducing the rate of or extending the time of payment of interest, or reducing any premium payable upon the redemption of any debt securities; or

reducing the percentage of debt securities, the holders of which are required to consent to any amendment, supplement, modification or waiver.

**Discharge**

Each indenture provides that we can elect to be discharged from our obligations with respect to one or more series of debt securities, except for specified obligations, including obligations to:

register the transfer or exchange of debt securities of the series;

replace stolen, lost or mutilated debt securities of the series;

maintain paying agencies;

hold monies for payment in trust;

recover excess money held by the debenture trustee;

compensate and indemnify the debenture trustee; and

appoint any successor trustee.

In order to exercise our rights to be discharged, we must deposit with the debenture trustee money or government obligations sufficient to pay all the principal of, any premium, if any, and interest on, the debt securities of the series on the dates payments are due.

**Form, Exchange and Transfer**

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We will issue the debt securities of each series only in fully registered form without coupons and, unless we provide otherwise in the applicable prospectus supplement, in denominations of \$1,000 and any integral multiple thereof. The indentures provide that we may issue debt securities of a series in temporary or permanent global form and as book-entry securities that will be deposited with, or on behalf of, The Depository Trust Company or another depository named by us and identified in a prospectus supplement with respect to that series. See "Legal Ownership of Securities" for a further description of the terms relating to any book-entry securities.

At the option of the holder, subject to the terms of the indentures and the limitations applicable to global securities described in the applicable prospectus supplement, the holder of the debt securities of

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any series can exchange the debt securities for other debt securities of the same series, in any authorized denomination and of like tenor and aggregate principal amount.

Subject to the terms of the indentures and the limitations applicable to global securities set forth in the applicable prospectus supplement, holders of the debt securities may present the debt securities for exchange or for registration of transfer, duly endorsed or with the form of transfer endorsed thereon duly executed if so required by us or the security registrar, at the office of the security registrar or at the office of any transfer agent designated by us for this purpose. Unless otherwise provided in the debt securities that the holder presents for transfer or exchange, we will impose no service charge for any registration of transfer or exchange, but we may require payment of any taxes or other governmental charges.

We will name in the applicable prospectus supplement the security registrar, and any transfer agent in addition to the security registrar, that we initially designate for any debt securities. We may at any time designate additional transfer agents or rescind the designation of any transfer agent or approve a change in the office through which any transfer agent acts, except that we will be required to maintain a transfer agent in each place of payment for the debt securities of each series.

If we elect to redeem the debt securities of any series, we will not be required to:

issue, register the transfer of, or exchange any debt securities of that series during a period beginning at the opening of business 15 days before the day of mailing of a notice of redemption of any debt securities that may be selected for redemption and ending at the close of business on the day of the mailing; or

register the transfer of or exchange any debt securities so selected for redemption, in whole or in part, except the unredeemed portion of any debt securities we are redeeming in part.

**Information Concerning the Debenture Trustee**

The debenture trustee, other than during the occurrence and continuance of an event of default under an indenture, undertakes to perform only those duties as are specifically set forth in the applicable indenture. Upon an event of default under an indenture, the debenture trustee must use the same degree of care as a prudent person would exercise or use in the conduct of his or her own affairs. Subject to this provision, the debenture trustee is under no obligation to exercise any of the powers given it by the indentures at the request of any holder of debt securities unless it is offered reasonable security and indemnity against the costs, expenses and liabilities that it might incur.

**Payment and Paying Agents**

Unless we otherwise indicate in the applicable prospectus supplement, we will make payment of the interest on any debt securities on any interest payment date to the person in whose name the debt securities, or one or more predecessor securities, are registered at the close of business on the regular record date for the interest.

We will pay principal of and any premium and interest on the debt securities of a particular series at the office of the paying agents designated by us, except that unless we otherwise indicate in the applicable prospectus supplement, we will make interest payments by check that we will mail to the holder or by wire transfer to certain holders. Unless we otherwise indicate in the applicable prospectus supplement, we will designate the corporate trust office of the debenture trustee in the City of New York as our sole paying agent for payments with respect to debt securities of each series. We will name in the applicable prospectus supplement any other paying agents that we initially designate for the debt securities of a particular series. We will maintain a paying agent in each place of payment for the debt securities of a particular series.

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All money we pay to a paying agent or the debenture trustee for the payment of the principal of or any premium or interest on any debt securities that remains unclaimed at the end of two years after such principal, premium or interest has become due and payable will be repaid to us, and the holder of the debt security thereafter may look only to us for payment thereof.

**Governing Law**

The indentures and the debt securities will be governed by and construed in accordance with the laws of the State of New York, except to the extent that the Trust Indenture Act of 1939 is applicable.

**Subordination of Subordinated Debt Securities**

The subordinated debt securities will be unsecured and will be subordinate and junior in priority of payment to certain of our other indebtedness to the extent described in a prospectus supplement. The subordinated indenture does not limit the amount of subordinated debt securities that we may issue, nor does it limit us from issuing any other secured or unsecured debt.

**DESCRIPTION OF WARRANTS**

We may issue warrants for the purchase of common stock, preferred stock and/or debt securities in one or more series. We may issue warrants independently or together with common stock, preferred stock and/or debt securities, and the warrants may be attached to or separate from these securities. While the terms summarized below will apply generally to any warrants that we may offer, we will describe the particular terms of any series of warrants in more detail in the applicable prospectus supplement. The terms of any warrants offered under a prospectus supplement may differ from the terms described below.

We will file as exhibits to the registration statement of which this prospectus is a part, or will incorporate by reference from reports that we file with the SEC, the form of warrant agreement, including a form of warrant certificate, that describes the terms of the particular series of warrants we are offering before the issuance of the related series of warrants. The following summaries of material provisions of the warrants and the warrant agreements are subject to, and qualified in their entirety by reference to, all the provisions of the warrant agreement and warrant certificate applicable to the particular series of warrants that we may offer under this prospectus. We urge you to read the applicable prospectus supplements related to the particular series of warrants that we may offer under this prospectus, as well as any related free writing prospectuses, and the complete warrant agreements and warrant certificates that contain the terms of the warrants.

**General**

We will describe in the applicable prospectus supplement the terms of the series of warrants being offered, including:

the offering price and aggregate number of warrants offered;

the currency for which the warrants may be purchased;

if applicable, the designation and terms of the securities with which the warrants are issued and the number of warrants issued with each such security or each principal amount of such security;

if applicable, the date on and after which the warrants and the related securities will be separately transferable;

in the case of warrants to purchase debt securities, the principal amount of debt securities purchasable upon exercise of one warrant and the price at, and currency in which, this principal amount of debt securities may be purchased upon such exercise;

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in the case of warrants to purchase common stock or preferred stock, the number of shares of common stock or preferred stock, as the case may be, purchasable upon the exercise of one warrant and the price at which these shares may be purchased upon such exercise;

the effect of any merger, consolidation, sale or other disposition of our business on the warrant agreements and the warrants;

the terms of any rights to redeem or call the warrants;

any provisions for changes to or adjustments in the exercise price or number of securities issuable upon exercise of the warrants;

the dates on which the right to exercise the warrants will commence and expire;

the manner in which the warrant agreements and warrants may be modified;

a discussion of any material or special United States federal income tax consequences of holding or exercising the warrants;

the terms of the securities issuable upon exercise of the warrants; and

any other specific terms, preferences, rights or limitations of or restrictions on the warrants.

Before exercising their warrants, holders of warrants will not have any of the rights of holders of the securities purchasable upon such exercise, including:

in the case of warrants to purchase debt securities, the right to receive payments of principal of, or premium, if any, or interest on, the debt securities purchasable upon exercise or to enforce covenants in the applicable indenture; or

in the case of warrants to purchase common stock or preferred stock, the right to receive dividends, if any, or payments upon our liquidation, dissolution or winding up or to exercise voting rights, if any.

**Exercise of Warrants**

Each warrant will entitle the holder to purchase the securities that we specify in the applicable prospectus supplement at the exercise price that we describe in the applicable prospectus supplement. Holders of the warrants may exercise the warrants at any time up to the specified time on the expiration date that we set forth in the applicable prospectus supplement. After the close of business on the expiration date, unexercised warrants will become void.

Holders of the warrants may exercise the warrants by delivering the warrant certificate representing the warrants to be exercised together with specified information, and paying the required amount to the warrant agent in immediately available funds, as provided in the applicable prospectus supplement. We will set forth on the reverse side of the warrant certificate and in the applicable prospectus supplement the information that the holder of the warrant will be required to deliver to the warrant agent.

Upon receipt of the required payment and the warrant certificate properly completed and duly executed at the corporate trust office of the warrant agent or any other office indicated in the applicable prospectus supplement, we will issue and deliver the securities purchasable upon such exercise. If fewer than all of the warrants represented by the warrant certificate are exercised, then we will issue a new warrant certificate

for the remaining amount of warrants. If we so indicate in the applicable prospectus supplement, holders of the warrants may surrender securities as all or part of the exercise price for warrants.

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**Governing Law**

Unless we provide otherwise in the applicable prospectus supplement, the warrants and warrant agreements will be governed by and construed in accordance with the laws of the State of New York.

**Enforceability of Rights by Holders of Warrants**

Each warrant agent will act solely as our agent under the applicable warrant agreement and will not assume any obligation or relationship of agency or trust with any holder of any warrant. A single bank or trust company may act as warrant agent for more than one issue of warrants. A warrant agent will have no duty or responsibility in case of any default by us under the applicable warrant agreement or warrant, including any duty or responsibility to initiate any proceedings at law or otherwise, or to make any demand upon us. Any holder of a warrant may, without the consent of the related warrant agent or the holder of any other warrant, enforce by appropriate legal action its right to exercise, and receive the securities purchasable upon exercise of, its warrants.

**DESCRIPTION OF UNITS**

We may issue, in one more series, units consisting of common stock, preferred stock, debt securities and/or warrants for the purchase of common stock, preferred stock and/or debt securities in any combination. While the terms we have summarized below will apply generally to any units that we may offer under this prospectus, we will describe the particular terms of any series of units in more detail in the applicable prospectus supplement. The terms of any units offered under a prospectus supplement may differ from the terms described below.

We will file as exhibits to the registration statement of which this prospectus is a part, or will incorporate by reference from reports that we file with the SEC, the form of unit agreement that describes the terms of the series of units we are offering, and any supplemental agreements, before the issuance of the related series of units. The following summaries of material terms and provisions of the units are subject to, and qualified in their entirety by reference to, all the provisions of the unit agreement and any supplemental agreements applicable to a particular series of units. We urge you to read the applicable prospectus supplements related to the particular series of units that we may offer under this prospectus, as well as any related free writing prospectuses and the complete unit agreement and any supplemental agreements that contain the terms of the units.

**General**

Each unit will be issued so that the holder of the unit is also the holder of each security included in the unit. Thus, the holder of a unit will have the rights and obligations of a holder of each included security. The unit agreement under which a unit is issued may provide that the securities included in the unit may not be held or transferred separately, at any time or at any time before a specified date.

We will describe in the applicable prospectus supplement the terms of the series of units being offered, including:

the designation and terms of the units and of the securities comprising the units, including whether and under what circumstances those securities may be held or transferred separately;

any provisions of the governing unit agreement that differ from those described below; and

any provisions for the issuance, payment, settlement, transfer or exchange of the units or of the securities comprising the units.

The provisions described in this section, as well as those described under "Description of Capital Stock," "Description of Debt Securities" and "Description of Warrants" will apply to each unit and to any common stock, preferred stock, debt security or warrant included in each unit, respectively.

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**Issuance in Series**

We may issue units in such amounts and in such numerous distinct series as we determine.

**Enforceability of Rights by Holders of Units**

Each unit agent will act solely as our agent under the applicable unit agreement and will not assume any obligation or relationship of agency or trust with any holder of any unit. A single bank or trust company may act as unit agent for more than one series of units. A unit agent will have no duty or responsibility in case of any default by us under the applicable unit agreement or unit, including any duty or responsibility to initiate any proceedings at law or otherwise, or to make any demand upon us. Any holder of a unit may, without the consent of the related unit agent or the holder of any other unit, enforce by appropriate legal action its rights as holder under any security included in the unit.

**Title**

We, and any unit agent and any of their agents, may treat the registered holder of any unit certificate as an absolute owner of the units evidenced by that certificate for any purpose and as the person entitled to exercise the rights attaching to the units so requested, despite any notice to the contrary. See "Legal Ownership of Securities" below.

**LEGAL OWNERSHIP OF SECURITIES**

We can issue securities in registered form or in the form of one or more global securities. We describe global securities in greater detail below. We refer to those persons who have securities registered in their own names on the books that we or any applicable trustee, depository or warrant agent maintain for this purpose as the "holders" of those securities. These persons are the legal holders of the securities. We refer to those persons who, indirectly through others, own beneficial interests in securities that are not registered in their own names, as "indirect holders" of those securities. As we discuss below, indirect holders are not legal holders, and investors in securities issued in book-entry form or in street name will be indirect holders.

**Book-Entry Holders**

We may issue securities in book-entry form only, as we will specify in the applicable prospectus supplement. This means securities may be represented by one or more global securities registered in the name of a financial institution that holds them as depository on behalf of other financial institutions that participate in the depository's book-entry system. These participating institutions, which are referred to as participants, in turn, hold beneficial interests in the securities on behalf of themselves or their customers.

Only the person in whose name a security is registered is recognized as the holder of that security. Securities issued in global form will be registered in the name of the depository or its participants. Consequently, for securities issued in global form, we will recognize only the depository as the holder of the securities, and we will make all payments on the securities to the depository. The depository passes along the payments it receives to its participants, which in turn pass the payments along to their customers who are the beneficial owners. The depository and its participants do so under agreements they have made with one another or with their customers; they are not obligated to do so under the terms of the securities.

As a result, investors in a book-entry security will not own securities directly. Instead, they will own beneficial interests in a global security, through a bank, broker or other financial institution that participates in the depository's book-entry system or holds an interest through a participant. As long as

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the securities are issued in global form, investors will be indirect holders, and not holders, of the securities.

**Street Name Holders**

We may terminate a global security or issue securities in non-global form. In these cases, investors may choose to hold their securities in their own names or in "street name." Securities held by an investor in street name would be registered in the name of a bank, broker or other financial institution that the investor chooses, and the investor would hold only a beneficial interest in those securities through an account he or she maintains at that institution.

For securities held in street name, we will recognize only the intermediary banks, brokers and other financial institutions in whose names the securities are registered as the holders of those securities, and we will make all payments on those securities to them. These institutions pass along the payments they receive to their customers who are the beneficial owners, but only because they agree to do so in their customer agreements or because they are legally required to do so. Investors who hold securities in street name will be indirect holders, not holders, of those securities.

**Legal Holders**

Our obligations, as well as the obligations of any applicable trustee and of any third parties employed by us or a trustee, run only to the legal holders of the securities. We do not have obligations to investors who hold beneficial interests in global securities, in street name or by any other indirect means. This will be the case whether an investor chooses to be an indirect holder of a security or has no choice because we are issuing the securities only in global form.

For example, once we make a payment or give a notice to the holder, we have no further responsibility for the payment or notice even if that holder is required, under agreements with depositary participants or customers or by law, to pass it along to the indirect holders but does not do so. Similarly, we may want to obtain the approval of the holders to amend an indenture, to relieve us of the consequences of a default or of our obligation to comply with a particular provision of the indenture or for other purposes. In such an event, we would seek approval only from the holders, and not the indirect holders, of the securities. Whether and how the holders contact the indirect holders is up to the holders.

**Special Considerations For Indirect Holders**

If you hold securities through a bank, broker or other financial institution, either in book-entry form or in street name, you should check with your own institution to find out:

how it handles securities payments and notices;

whether it imposes fees or charges;

how it would handle a request for the holders' consent, if ever required;

whether and how you can instruct it to send you securities registered in your own name so you can be a holder, if that is permitted in the future;

how it would exercise rights under the securities if there were a default or other event triggering the need for holders to act to protect their interests; and

if the securities are in book-entry form, how the depositary's rules and procedures will affect these matters.



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**Global Securities**

A global security is a security that represents one or any other number of individual securities held by a depository. Generally, all securities represented by the same global securities will have the same terms.

Each security issued in book-entry form will be represented by a global security that we deposit with and register in the name of a financial institution or its nominee that we select. The financial institution that we select for this purpose is called the depository. Unless we specify otherwise in the applicable prospectus supplement, The Depository Trust Company, New York, New York, known as DTC, will be the depository for all securities issued in book-entry form.

A global security may not be transferred to or registered in the name of anyone other than the depository, its nominee or a successor depository, unless special termination situations arise. We describe those situations below under "Special Situations When a Global Security Will Be Terminated." As a result of these arrangements, the depository, or its nominee, will be the sole registered owner and holder of all securities represented by a global security, and investors will be permitted to own only beneficial interests in a global security. Beneficial interests must be held by means of an account with a broker, bank or other financial institution that in turn has an account with the depository or with another institution that does. Thus, an investor whose security is represented by a global security will not be a holder of the security, but only an indirect holder of a beneficial interest in the global security.

If the prospectus supplement for a particular security indicates that the security will be issued in global form only, then the security will be represented by a global security at all times unless and until the global security is terminated. If termination occurs, we may issue the securities through another book-entry clearing system or decide that the securities may no longer be held through any book-entry clearing system.

**Special Considerations For Global Securities**

The rights of an indirect holder relating to a global security will be governed by the account rules of the investor's financial institution and of the depository, as well as general laws relating to securities transfers. We do not recognize an indirect holder as a holder of securities and instead deal only with the depository that holds the global security.

If securities are issued only in the form of a global security, an investor should be aware of the following:

an investor cannot cause the securities to be registered in his or her name, and cannot obtain non-global certificates for his or her interest in the securities, except in the special situations we describe below;

an investor will be an indirect holder and must look to his or her own bank or broker for payments on the securities and protection of his or her legal rights relating to the securities, as we describe above;

an investor may not be able to sell interests in the securities to some insurance companies and to other institutions that are required by law to own their securities in non-book-entry form;

an investor may not be able to pledge his or her interest in a global security in circumstances where certificates representing the securities must be delivered to the lender or other beneficiary of the pledge in order for the pledge to be effective;

the depository's policies, which may change from time to time, will govern payments, transfers, exchanges and other matters relating to an investor's interest in a global security;

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we and any applicable trustee have no responsibility for any aspect of the depositary's actions or for its records of ownership interests in a global security, nor do we or any applicable trustee supervise the depositary in any way;

the depositary may, and we understand that DTC will, require that those who purchase and sell interests in a global security within its book-entry system use immediately available funds, and your broker or bank may require you to do so as well; and

financial institutions that participate in the depositary's book-entry system, and through which an investor holds its interest in a global security, may also have their own policies affecting payments, notices and other matters relating to the securities.

There may be more than one financial intermediary in the chain of ownership for an investor. We do not monitor and are not responsible for the actions of any of those intermediaries.

**Special Situations When a Global Security Will Be Terminated**

In a few special situations described below, the global security will terminate and interests in it will be exchanged for physical certificates representing those interests. After that exchange, the choice of whether to hold securities directly or in street name will be up to the investor. Investors must consult their own banks or brokers to find out how to have their interests in securities transferred to their own name, so that they will be direct holders. We have described the rights of holders and street name investors above.

Unless we provide otherwise in the applicable prospectus supplement, the global security will terminate when the following special situations occur:

if the depositary notifies us that it is unwilling, unable or no longer qualified to continue as depositary for that global security and we do not appoint another institution to act as depositary within 90 days;

if we notify any applicable trustee that we wish to terminate that global security; or

if an event of default has occurred with regard to securities represented by that global security and has not been cured or waived.

The prospectus supplement may also list additional situations for terminating a global security that would apply only to the particular series of securities covered by the applicable prospectus supplement. When a global security terminates, the depositary, and not we or any applicable trustee, is responsible for deciding the names of the institutions that will be the initial direct holders.

**PLAN OF DISTRIBUTION**

We may sell the securities from time to time pursuant to underwritten public offerings, negotiated transactions, block trades or a combination of these methods. We may sell the securities to or through underwriters or dealers, through agents, or directly to one or more purchasers. We may distribute securities from time to time in one or more transactions:

at a fixed price or prices, which may be changed;

at market prices prevailing at the time of sale;

at prices related to such prevailing market prices; or

at negotiated prices.

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A prospectus supplement or supplements will describe the terms of the offering of the securities, including:

the name or names of the underwriters, if any;

the purchase price of the securities and the proceeds we will receive from the sale;

any over-allotment options under which underwriters may purchase additional securities from us;

any agency fees or underwriting discounts and other items constituting agents' or underwriters' compensation;

any public offering price;

any discounts or concessions allowed or reallocated or paid to dealers; and

any securities exchange or market on which the securities may be listed.

Only underwriters named in the prospectus supplement will be underwriters of the securities offered by the prospectus supplement.

If underwriters are used in the sale, they will acquire the securities for their own account and may resell the securities from time to time in one or more transactions at a fixed public offering price or at varying prices determined at the time of sale. The obligations of the underwriters to purchase the securities will be subject to the conditions set forth in the applicable underwriting agreement. We may offer the securities to the public through underwriting syndicates represented by managing underwriters or by underwriters without a syndicate. Subject to certain conditions, the underwriters will be obligated to purchase all of the securities offered by the prospectus supplement, other than securities covered by any over-allotment option. Any public offering price and any discounts or concessions allowed or reallocated or paid to dealers may change from time to time. We may use underwriters with whom we have a material relationship. We will describe in the prospectus supplement, naming the underwriter, the nature of any such relationship.

We may sell securities directly or through agents we designate from time to time. We will name any agent involved in the offering and sale of securities and we will describe any commissions we will pay the agent in the prospectus supplement. Unless the prospectus supplement states otherwise, our agent will act on a best-efforts basis for the period of its appointment.

We may authorize agents or underwriters to solicit offers by certain types of institutional investors to purchase securities from us at the public offering price set forth in the prospectus supplement pursuant to delayed delivery contracts providing for payment and delivery on a specified date in the future. We will describe the conditions to these contracts and the commissions we must pay for solicitation of these contracts in the prospectus supplement.

We may provide agents and underwriters with indemnification against civil liabilities, including liabilities under the Securities Act, or contribution with respect to payments that the agents or underwriters may make with respect to these liabilities. Agents and underwriters may engage in transactions with, or perform services for, us in the ordinary course of business.

All securities we may offer, other than common stock, will be new issues of securities with no established trading market. Any underwriters may make a market in these securities, but will not be obligated to do so and may discontinue any market making at any time without notice. We cannot guarantee the liquidity of the trading markets for any securities.

Any underwriter may engage in over-allotment, stabilizing transactions, short-covering transactions and penalty bids in accordance with Regulation M under the Exchange Act. Over-allotment involves sales in excess of the offering size, which create a short position. Stabilizing transactions permit bids to purchase the underlying security so long as the stabilizing bids do not exceed a specified maximum



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price. Syndicate-covering or other short-covering transactions involve purchases of the securities, either through exercise of the over-allotment option or in the open market after the distribution is completed, to cover short positions. Penalty bids permit the underwriters to reclaim a selling concession from a dealer when the securities originally sold by the dealer are purchased in a stabilizing or covering transaction to cover short positions. Those activities may cause the price of the securities to be higher than it would otherwise be. If commenced, the underwriters may discontinue any of the activities at any time.

Any underwriters that are qualified market makers on the Nasdaq Global Select Market may engage in passive market making transactions in the common stock on the Nasdaq Global Select Market in accordance with Regulation M under the Exchange Act, during the business day prior to the pricing of the offering, before the commencement of offers or sales of the common stock. Passive market makers must comply with applicable volume and price limitations and must be identified as passive market makers. In general, a passive market maker must display its bid at a price not in excess of the highest independent bid for such security; if all independent bids are lowered below the passive market maker's bid, however, the passive market maker's bid must then be lowered when certain purchase limits are exceeded. Passive market making may stabilize the market price of the securities at a level above that which might otherwise prevail in the open market and, if commenced, may be discontinued at any time.

In compliance with guidelines of the Financial Industry Regulatory Authority, or FINRA, the maximum consideration or discount to be received by any FINRA member or independent broker dealer may not exceed 8% of the aggregate amount of the securities offered pursuant to this prospectus and any applicable prospectus supplement.

#### **LEGAL MATTERS**

The validity of the securities being offered by this prospectus will be passed upon by Morrison & Foerster LLP, San Diego, California.

#### **EXPERTS**

Grant Thornton LLP, independent registered public accounting firm, has audited our consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 28, 2008 as set forth in their report, which is incorporated by reference in this prospectus and elsewhere in the registration statement. Our consolidated financial statements are incorporated by reference in reliance on Grant Thornton LLP's reports, given on its authority as experts in accounting and auditing.

#### **WHERE YOU CAN FIND ADDITIONAL INFORMATION**

We file annual, quarterly and special reports, proxy statements and other information with the SEC. You may read and copy any document we file at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for more information about the operation of the public reference room. The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, including Kratos Defense & Security Solutions, Inc. The SEC's Internet site can be found at [www.sec.gov](http://www.sec.gov).

The SEC allows us to incorporate by reference the information we file with it, which means that we can disclose important information to you by referring you to another document that we have filed separately with the SEC. You should read the information incorporated by reference because it is an

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important part of this prospectus. We incorporate by reference the following information or documents that we have filed with the SEC (Commission File No. 000-27231):

our Annual Report on Form 10-K for the fiscal year ended December 28, 2008 filed with the SEC on March 10, 2009;

our Quarterly Report on Form 10-Q for the fiscal quarter ended March 29, 2009 filed with the SEC on May 12, 2009;

our Quarterly Report on Form 10-Q for the fiscal quarter ended June 28, 2009 filed with the SEC on August 6, 2009;

our Definitive Proxy Statement on Schedule 14A filed with the SEC on April 27, 2009;

our Current Reports on Form 8-K filed with the SEC on December 31, 2008, January 23, 2009, February 13, 2009, June 10, 2009, August 6, 2009 (with respect to Item 3.03 only) and August 13, 2009;

the description of our Common Stock contained in our Registration Statement on Form 8-A (File No. 000-27231), filed under Section 12(g) of the Exchange Act on September 3, 1999, including any subsequent amendment or report filed for the purpose of amending such description; and

the description of the purchase rights for Series C Preferred Stock, par value \$0.001 per share, contained in our Registration Statement on Form 8-A (File No. 000-27231), initially filed under Section 12(g) of the Exchange Act on December 17, 2004, including any subsequent amendment or report filed for the purpose of amending such description.

Any information in any of the foregoing documents will automatically be deemed to be modified or superseded to the extent that information in this prospectus or in a later filed document that is incorporated or deemed to be incorporated herein by reference modifies or replaces such information.

We also incorporate by reference any future filings (other than current reports furnished under Item 2.02 or Item 7.01 of Form 8-K and exhibits filed on such form that are related to such items) made with the SEC pursuant to Sections 13(a), 13(c), 14 or 15(d) of the Exchange Act, until we file a post-effective amendment that indicates the termination of the offering of the securities made by this prospectus. Information in such future filings updates and supplements the information provided in this prospectus. Any statements in any such future filings will automatically be deemed to modify and supersede any information in any document we previously filed with the SEC that is incorporated or deemed to be incorporated herein by reference to the extent that statements in the later filed document modify or replace such earlier statements.

We will provide to each person, including any beneficial owner, to whom a prospectus is delivered, without charge upon written or oral request, a copy of any or all of the documents that are incorporated by reference into this prospectus but not delivered with the prospectus, including exhibits which are specifically incorporated by reference into such documents. Requests should be directed to: Kratos Defense & Security Solutions, Inc., Attention: Investor Relations, 4810 Eastgate Mall, San Diego, California, 92121, telephone (858) 812-7300.

Messrs. Gulling, Olafson, and Winterbottom. Under their respective agreements, Mr. Gulling will serve as Executive Vice President and Chief Financial Officer of the Company and Chief Financial Officer of West Bank, Mr. Olafson will serve as Executive Vice President and Chief Risk Officer of the Company and West Bank, and Mr. Winterbottom will serve as Executive Vice President of the Company and President of West Bank. Each individual will also serve as a member of the board of directors of West Bank. The initial term under each agreement ends on December 31, 2014, but the agreements renew automatically for one-year terms on January 1, 2014 and on each January 1 thereafter. Messrs. Gulling, Olafson, and Winterbottom are each entitled to a minimum annual salary pursuant to their agreements, as well as annual performance bonuses and participation in the Company's benefit plans. Under the agreements, upon an involuntary termination of the respective executive's employment, the executive will be entitled to severance benefits contingent upon his execution of a general release of claims. Under the agreements, Messrs. Gulling, Olafson, and Winterbottom will be subject to non-compete and non-solicit restrictive covenants following termination of employment.

#### 2012 Equity Incentive Plan - Acceleration of Awards

The 2012 Plan provides for possible accelerated vesting of awards granted to all participants, including our named executive officers, in certain circumstances. Under the 2012 Plan, and to the extent not provided otherwise in the agreements setting forth the terms of the award, vesting will be accelerated for outstanding awards upon a "change in control" of the Company (as defined in the 2012 Plan) if the awards are not assumed or otherwise equitably converted into comparable awards by the acquiring company. If the awards are assumed by the acquiror and a participant's employment is terminated without "cause" or a participant resigns for "good reason," the participant's awards will become vested (this is what is known as a "double trigger" approach). We adopted this approach, rather than providing for vesting solely upon a change in control (a "single trigger" approach) because we believe that the double trigger provides adequate employment protection and reduces potential costs associated with various strategic transactions for the benefit of the stockholders. Further, the award agreements under the 2012 Plan generally provide that vesting will be accelerated for outstanding awards upon the respective participant's disability or death.

#### No Tax Gross-Ups

Under Section 280G of the Internal Revenue Code, an executive may be subject to excise taxes on certain benefits received in relation to a change in control of the Company. While many companies provide excise tax gross-ups to executives to place the executive in the same tax position as if the excise tax did not apply, we do not believe it is appropriate to provide this type of protection to any executive.

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Compensation Process

The Compensation Committee has broad discretion in overseeing our compensation programs. It reviews each element of compensation for each of our named executive officers at least once each year and makes a final determination regarding any adjustments to their current compensation structure and levels after considering a number of factors. The Compensation Committee takes into account the scope of the named executive officer's responsibilities, performance and experience, as well as competitive compensation levels in reviewing compensation. During the annual review process, the Compensation Committee also reviews our full-year financial results against other banking organizations and reviews the structure of our compensation programs relative to sound risk management.

In particular, our executive compensation decisions consider several factors of which the primary are:

- Key financial measurements;
- Strategic initiatives related to our business;
- Achievement of specific operational goals relating to the executive's area of oversight;
- Compensation of other Company executives; and
- Compensation of peer group executives.

Consulting Assistance

Under its charter, the Compensation Committee has the authority to retain its own compensation consultants. In July 2011, the Compensation Committee retained F.W. Cook to provide the Compensation Committee with independent, objective analysis and professional opinions on executive compensation matters. F.W. Cook is independent, reports directly to the Chair of the Compensation Committee, and performs no other work for the Company. During 2011, F.W. Cook assisted the Committee in the review of the total compensation program, including gathering and analyzing market data for compensation paid for similar positions at companies with which we compete for executive talent. F.W. Cook also provided input on marketplace trends and best practices relating to competitive pay levels, as well as developments in regulatory and technical matters. During 2012, the Compensation Committee again retained F.W. Cook to continue to review and monitor our executive compensation program in light of trends in market practice, regulatory developments, and internal considerations.

Role of Executive Officers

Various members of management facilitate the Compensation Committee's consideration of compensation for our named executive officers by providing information for the Committee's review. This includes, among other items, financial results and analysis, performance evaluations, compensation provided to our named executive officers, technical and regulatory considerations, and input on program design and possible modifications.

Market Benchmarking

Market pay practices are one of many factors we consider in setting executive pay levels and designing compensation programs. In 2011, we gathered information on pay levels and practices for a group of publicly traded companies selected based on their business focus, scope and location of operations, size, and other considerations. A group of 12 benchmark companies was jointly selected by our Consultant and management and approved by the Compensation Committee in 2011. In January 2012, four additional companies were added to the group at the Compensation Committee's direction. The Company's peer group consists of 16 financial institutions, as listed below, that are similar in regional presence, asset size, and business model. The Company is in the middle of the group in terms of size.

BankFinancial Corporation

Horizon Bancorp

MidWestOne Financial Group, Inc.

Baylake Corp.	Isabella Bank Corporation	MutualFirst Financial, Inc.
CFS Bancorp, Inc.	Macatawa Bank Corporation	NASB Financial, Inc.
Firstbank Corporation	Mercantile Bank Corporation	Pulaski Financial Corp.
First Mid-Illinois Bancshares, Inc.	MetroCorp Bancshares, Inc	QCR Holdings, Inc.
Hills Bancorporation		

The companies in the group will be reviewed and evaluated on a regular basis.

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Analysis of 2012 Compensation

Consistent with our philosophy of linking compensation to performance, compensation for our named executive officers in 2012 was based on our business results. As noted above, the Company returned to a level of profitability that puts us in the top quartile of bank holding companies in the United States with assets between \$1 billion and \$3 billion (according to the September 2012 Bank Holding Company Performance Report). This section discusses the compensation actions that were taken in 2012 for our named executive officers, as reported in the Executive Compensation section below.

Base Salary

Salaries for our named executive officers for 2012 were set as follows in light of the factors mentioned above: Mr. Nelson - \$350,000; Mr. Gulling - \$247,000; Mr. Olafson - \$247,000; and Mr. Winterbottom - \$247,000. Salaries for 2013 remain at 2012 levels.

Annual Incentive Bonus

For 2012, the maximum bonus percentage for our named executive officers was increased to 60% of base salary in light of historical market practices, the Company's performance, and the continuing development of the executive team.

Based on peer group analysis using September 30, 2012 data, we believe Company results likely will be at or above the 75th percentile of our peer group. As such, we believe our named executive officers will be eligible to receive a cash bonus with respect to 2012. However, because the ultimate amount of the cash bonus is based on the Company's performance compared to that of the peer groups for the entire year and the Committee's qualitative analysis, the amount of the cash bonus payments will not be known until after the peer group institutions have reported their financial results for 2012.

Long-Term Stock Incentives

During 2012, our Compensation Committee made two separate equity grants to our named executive officers comprised solely of restricted stock units. The first grant, made in May 2012, was a one-time grant intended to bring our equity compensation pay practices more in line with market practice and our peer group. In part, this grant was also intended to provide our named executive officers with compensation they could have earned during the TARP period even after applying the TARP compensation limitations. The Committee chose to wait until after we were out of TARP to make these awards. On June 29, 2011, we redeemed all of the preferred stock that we sold to the Treasury pursuant to TARP. The May 2012 grant was in the form of restricted stock units and the terms of the grant are intended to satisfy those portions of the TARP compensation rules that otherwise would have applied had the grant been made as a long-term incentive under the TARP compensation rules during the TARP period. The May 2012 grant will vest in full in May 2014.

The second equity grant was made in August 2012 when Mr. Nelson was awarded 8,233 restricted stock units and Messrs. Gulling, Olafson, and Winterbottom each received 5,810 restricted stock units. This grant was intended to be an annual equity award with respect to 2012 and is intended to be a part of a broader annual award program pursuant to which the Compensation Committee can continue to further align our named executive officers' interests with those of our stockholders. The equity awards were in the form of restricted stock units vesting in annual installments tied to continued service over a period of five years. This approach is designed to align executives' interests with the interests of stockholders, provide a long-term planning horizon, mitigate excessive risk-taking, and retain participants by providing a compensation package that is competitive.

We also anticipate granting equity awards for 2013.

#### Regulatory Considerations

As a publicly traded financial institution, the Company must contend with several often overlapping layers of regulations when considering and implementing compensation-related decisions. These regulations do not set specific parameters within which compensation decisions must be made, but do require the Company and the Compensation Committee to be mindful of the risks that often go hand-in-hand with compensation programs designed to incentivize the achievement of better than average performance. While the regulatory focus on risk assessment has been heightened over the last several years, the incorporation of general concepts of risk assessment into compensation decisions is not a recent development.

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Under its long-standing Interagency Guidelines Establishing Standards for Safety and Soundness, the FDIC has held that excessive compensation is prohibited as an unsafe and unsound practice. In describing a framework within which to make a determination as to whether compensation is to be considered excessive, the FDIC has indicated that financial institutions should consider whether aggregate cash amounts paid, or noncash benefits provided, to employees are unreasonable or disproportionate to the services performed by an employee. The FDIC encourages financial institutions to review an employee's compensation history and to consider internal pay equity, and, as appropriate, to consider benchmarking compensation to peer groups. Finally, the FDIC provides that such an assessment must be made in light of the institution's overall financial condition.

In the summer of 2010, the various financial institution regulatory agencies worked together to issue additional guidance, Guidance on Sound Incentive Compensation Policies, that was, in many respects, intended to serve as a complement to the Safety and Soundness standards. As its title would imply, the joint agency guidance sets forth a framework for assessing the soundness of incentive compensation plans, programs, and arrangements maintained by financial institutions. The joint agency guidance is narrower in scope than the Safety and Soundness standards because it applies only to senior executive officers and those other individuals who, either alone or as a group, could pose a material risk to the institution. With respect to those identified individuals, the joint agency guidance is intended to focus the institution's attention on balanced risk-taking incentives, compatibility with effective controls, and risk management, with a focus on general principles of strong corporate governance.

Also, once further risk assessment guidelines and procedures, as required under the Dodd-Frank Act, are finalized by the financial institution regulatory agencies and the SEC, the Company expects that it will also be subject to those further guidelines and procedures. However, initial guidance respecting the Dodd-Frank Act risk assessment guidelines and procedures was issued during 2011 and, in large part that guidance restates the frameworks set forth in the Safety and Soundness standards and joint agency guidance described above.

Finally, in addition to the foregoing, as a publicly traded corporation, the Company is also subject to the SEC's rules regarding risk assessment. Those rules require a publicly traded company to determine whether any of its existing incentive compensation plans, programs, or arrangements creates risks that are reasonably likely to have a material adverse effect on the company. We do not believe that our incentive compensation plans, programs, or arrangements create risks that are reasonably likely to have a material adverse effect on the Company.

The Compensation Committee believes that a sensible approach to balancing risk-taking and rewarding reasonable, but not necessarily easily attainable, goals has always been a component of its overall assessment of the compensation plans, programs, and arrangements it has established for the Company's named executive officers. In this regard, the Compensation Committee has revisited the components of the frameworks set forth in the Safety and Soundness standards and the joint agency guidance as an effective tool for conducting its own assessment of the balance between risk and reward built into the Company's compensation programs for named executive officers. In addition, the Committee continues to anticipate final guidance under the Dodd-Frank Act and will be prepared to incorporate into its risk assessment procedures any new guidelines and procedures as may be necessary or appropriate.

In making decisions about executive compensation, in addition to the above, we also consider the impact of other regulatory provisions, including the provisions of Section 162(m) of the Code limiting the tax deductibility of certain compensation unless it is considered performance-based under Section 409A of the Code regarding nonqualified deferred compensation, and the change-in-control provisions of Section 280G of the Code. In making decisions about executive compensation, we also consider how various elements of compensation will impact our financial results. For example, we consider the impact of FASB ASC Topic 718, which requires us to recognize the compensation cost of grants of equity awards based upon the grant date fair value of those awards.

Share Ownership and Retention Guidelines

We believe that our named executive officers and non-employee directors should have a significant equity interest in the Company. To promote such equity ownership and further align the interests of our executives and directors with our stockholders, we adopted share retention and ownership guidelines for our named executive officers equal to three times salary and for our directors equal to three times annual cash retainer. Until the stock ownership guidelines are met, the executives and directors are expected to retain 50% of any applicable shares received (on a net after tax basis) under our equity compensation program. The program is subject to periodic review by the Compensation Committee.

The Company has had in place for several years an insider trading policy that permits open market transactions in Company stock beginning 48 hours after quarterly earnings have been made public until the 10th day of the third month in the quarter. In addition, our named executive officers may purchase Company stock through payroll deductions under our Employee Savings and Stock Ownership Plan. Changes to purchases under the Employee Savings and Stock Ownership Plan may only be done during the period when open market transactions are permitted. The insider trading policy requires named executive officers to request approval prior to entering into any hedging transactions involving the Company's securities.

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## Summary Compensation Table

The following table provides information concerning total compensation earned or paid for services rendered in the year ended December 31, 2012, to those serving as our Chief Executive Officer, our Chief Financial Officer, and our other most highly compensated executive policymaking officers (of which we had two). These gentlemen were the Company's named executive officers during 2012. Compensation for 2011 and 2010 is also presented for these gentlemen, as they were our named executive officers in those years as well. In 2012, West Bank, rather than the Company, paid Messrs. Nelson, Gulling, Olafson, and Winterbottom.

Name and Principal Positions	Year	Salary (1)	Bonus (2)	Stock Awards (3)	Non-Equity Incentive Plan Compensation (4)	All Other Compensation (5)	Total (6)
David D. Nelson President and Chief Executive Officer of the Company; Chairman and Chief Executive Officer of West Bank	2012	\$350,000	\$7,000	(7) \$70,000	\$—	\$28,832	\$455,832
	2011	275,000	74,250	(8) 68,750	(8) —	36,327	454,327
	2010	203,078	125,000	—	—	50,750	378,828
Douglas R. Gulling Executive Vice President and Chief Financial Officer of the Company; Director and Chief Financial Officer of West Bank	2012	\$247,000	\$4,940	(7) \$49,400	\$—	\$30,486	\$331,826
	2011	225,000	49,500	(8) 45,000	(8) —	27,010	346,510
	2010	214,789	—	—	—	18,603	233,392
Harlee N. Olafson Executive Vice President and Chief Risk Officer of the Company; Director, Executive Vice President, and Chief Risk Officer of West Bank	2012	\$247,000	\$4,940	(7) \$49,400	\$—	\$30,486	\$331,826
	2011	210,000	88,200	(8) —	—	23,359	321,559
	2010	84,000	30,000	—	—	15,877	129,877
Brad L. Winterbottom Executive Vice President of the Company; Director and President of West Bank	2012	\$247,000	\$4,940	(7) \$49,400	\$—	\$30,486	\$331,826
	2011	225,000	49,500	(8) 45,000	(8) —	30,229	349,729
	2010	214,789	—	—	—	22,042	236,831

(1) Amounts reflect base salary earned during the year, before any deferrals, and including salary increases during the year, if any.

(2) Amounts are shown in the year earned.

(3)

The amounts set forth in the "Stock Awards" column reflect the grant date fair value of awards granted during the year ended December 31, 2012, in accordance with FASB ASC Topic 718. The assumptions used in calculating these amounts are set forth in Note 10 to our consolidated financial statements for the year ended December 31, 2012, which is located on page 86 of our Annual Report on Form 10-K.

Annual bonuses for 2012 performance cannot be determined until peer company financial information is available.

Based upon our results and the results of our peers as of September 30, 2012, annual bonuses for 2012 would be (4) paid out at the following maximum levels: Mr. Nelson - \$210,000; Mr. Gulling - \$148,200; Mr. Olafson - \$148,200; and Mr. Winterbottom - \$148,200. The final determination of amounts earned for 2012 will be made after the companies included in the benchmarking peer group have filed their final results for 2012.

Consists entirely of contributions made by the Company on behalf of the named executive officer to the Company's (5) Employee Savings and Stock Ownership Plan (including 401(k) matches and discretionary plan contributions for 2012) except for the following amounts for 2012, which represent premiums on group term life insurance coverage: Nelson - \$1,140; Gulling - \$846; Olafson - \$846; and Winterbottom - \$846.

If annual bonuses for 2012 are paid out at maximum levels, as reflected in footnote (4) above, the total (6) compensation amounts reflected in this column will be as follows: Mr. Nelson - \$665,832; Mr. Gulling - \$480,026; Mr. Olafson - \$480,026; and Mr. Winterbottom - \$480,026.

(7) Consists of a holiday bonus equal to 2% of annual salary paid to all officers and employees of West Bank.

Because we were subject to the TARP limitations for approximately six months of 2011, approximately 50% of (8) annual bonuses for 2011 were paid in cash and the remaining amounts were paid in 2012 in the form of restricted stock units under the 2012 Plan that will vest 100% on May 17, 2014, subject to continued service. Mr. Olafson was not subject to TARP limitations and, therefore, received 100% of his 2011 bonus in cash.

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## Grants of Plan-Based Awards

The following table sets forth certain information concerning grants of plan-based awards made to our named executive officers during 2012. All restricted stock unit grants reflected in the table were made under the West Bancorporation, Inc. 2012 Equity Incentive Plan, which is described in more detail in the CD&A.

Name	Type of Award	Grant Date	Compensation Committee Approval Date	Estimated Future Payouts Under Non-Equity Incentive Plan Awards			All Other Grant Stock Awards: Number of Shares of Stock or Units (#)	Grant Date Fair Value of Stock Awards (\$)
				Threshold (\$)	Target (\$)	Maximum (\$)		
David D. Nelson	Annual Bonus	—	—	\$70,000	\$140,000	\$210,000	—	\$—
	Restricted Stock Units	05/17/12	05/17/12	—	—	—	8,249	68,750
	Restricted Stock Units	08/01/12	07/23/12	—	—	—	8,233	70,000
Douglas R. Gulling	Annual Bonus	—	—	\$49,400	\$98,800	\$148,200	—	—
	Restricted Stock Units	05/17/12	05/17/12	—	—	—	5,399	45,000
	Restricted Stock Units	08/01/12	07/23/12	—	—	—	5,810	49,400
Harlee N. Olafson	Annual Bonus	—	—	\$49,400	\$98,800	\$148,200	—	—
	Restricted Stock Units	08/01/12	07/23/12	—	—	—	5,810	49,400
Brad L. Winterbottom	Annual Bonus	—	—	\$49,400	\$98,800	\$148,200	—	—
	Restricted Stock Units	05/17/12	05/17/12	—	—	—	5,399	45,000
	Restricted Stock Units	08/01/12	07/23/12	—	—	—	5,810	49,400

## Annual Bonuses

Annual bonuses for our named executive officers for 2012 will be based on quantitative and qualitative analyses. The quantitative analysis includes the Company's relative performance against a peer group of other banking organizations. The qualitative analysis will include any and all items deemed relevant by the Compensation Committee including, for example, regulatory action and changes in dividends. Based on the Compensation Committee's evaluation, it may increase or decrease the bonuses indicated from the peer comparison as it deems appropriate in its sole discretion, with all determinations by the Committee being final. Positive Company earnings are required for any bonuses to be paid to our named executive officers.

## Restricted Stock Units

Because we were subject to the TARP limitations for approximately six months of 2011, approximately 50% of annual bonuses for 2011 were paid in cash and the remaining amounts were paid in 2012 in the form of restricted stock units granted on May 17, 2012 that will vest 100% on May 17, 2014, subject to continued service. These restricted stock units are reflected in the Grants of Plan-Based Awards table above for Messrs. Nelson, Gulling, and Winterbottom. Mr. Olafson was not subject to TARP limitations and, therefore, received 100% of his 2011 bonus in cash.

In July 2012, the Compensation Committee approved equity grants for our named executive officers comprised solely of restricted stock units. Mr. Nelson was awarded 8,233 restricted stock units and Messrs. Gulling, Olafson, and Winterbottom each received 5,810 restricted stock units. Each of these grants vest 20% per year subject to continued service.

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## Outstanding Equity Awards at Fiscal Year End

The following table sets forth information concerning non-vested restricted stock units held as of December 31, 2012, by our named executive officers. Market values for outstanding restricted stock units are based on the closing price of our stock on December 31, 2012 (the last trading day of the year) of \$10.78.

Name	Stock Awards	
	Number of Shares or Units of Stock That Have Not Vested	Market Value of Shares or Units of Stock That Have Not Vested
David D. Nelson	16,482 <sup>(1)</sup>	\$177,676
Douglas R. Gulling	11,209 <sup>(2)</sup>	120,833
Harlee N. Olafson	5,810 <sup>(3)</sup>	62,632
Brad L. Winterbottom	11,209 <sup>(2)</sup>	120,833

Reflects 8,249 restricted stock units granted on May 17, 2012, which vest fully on May 17, 2014; and 8,233

(1) restricted stock units granted on August 1, 2012, which vest in five equal annual installments beginning on the first anniversary of the grant date.

Reflects 5,399 restricted stock units granted on May 17, 2012, which vest fully on May 17, 2014; and 5,810

(2) restricted stock units that were granted on August 1, 2012, which vest in five equal annual installments beginning on the first anniversary of the grant date.

(3) Reflects 5,810 restricted stock units granted on August 1, 2012, which vest in five equal annual installments beginning on the first anniversary of the grant date.

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## Potential Payments Upon Termination or Change in Control

The table below sets forth the estimated amount of compensation payable to each of the named executive officers upon termination of such officer's employment in the event of (1) the officer's disability or death, (2) termination by the Company without cause or by the officer for good reason, in each case other than in connection with a change in control, and (3) termination by the Company without cause or by the officer for good reason, in each case in connection with a change in control. The amounts shown assume the termination was effective as of December 31, 2012, and that the price of Company stock as of termination was the closing price of \$10.78 on December 31, 2012 (the last trading day of the year). The actual amounts to be paid can be determined only following the named executive officer's termination. We generally do not provide any benefits to our named executive officers solely as a result of a change in control.

Name	Type of Payment	Payments Upon Disability or Death	Payments Upon Termination by the Company without Cause or by the Executive for Good Reason-No Change in Control	Payments Upon Termination by the Company without Cause or by the Executives for Good Reason-Change in Control
David D. Nelson	Cash Severance	\$ 159,038	\$ 1,134,038	\$ 1,621,538
	Continuation of Insurance Benefits	—	15,039	15,039
	Acceleration of Stock Awards	177,676	—	177,676
	Total	\$ 336,714	\$ 1,149,077	\$ 1,814,253
Douglas R. Gulling	Cash Severance	\$ 109,000	\$ 446,000	\$ 783,000
	Continuation of Insurance Benefits	—	9,711	14,567
	Acceleration of Stock Awards	120,833	—	120,833
	Total	\$ 229,833	\$ 455,711	\$ 918,400
Harlee N. Olafson	Cash Severance	\$ 94,925	\$ 425,925	\$ 756,925
	Continuation of Insurance Benefits	—	10,026	15,039
	Acceleration of Stock Awards	62,632	—	62,632
	Total	\$ 157,557	\$ 435,951	\$ 834,596
Brad L. Winterbottom	Cash Severance	\$ 109,000	\$ 446,000	\$ 783,000
	Continuation of Insurance Benefits	—	10,026	15,039
	Acceleration of Stock Awards	120,833	—	120,833
	Total	\$ 229,833	\$ 456,026	\$ 918,872

## Termination and Change in Control Benefits under Employment Agreement with Mr. Nelson

We entered into a new employment agreement with Mr. Nelson, effective July 23, 2012, which superseded his prior employment agreement in its entirety. Mr. Nelson will serve as the President and Chief Executive Officer of the Company and as the Chief Executive Officer of West Bank under the agreement, as well as a member of the board of directors of both entities. The initial term under Mr. Nelson's agreement ends on December 31, 2015, but the agreement renews automatically for one-year terms on January 1, 2015, and on each January 1 thereafter unless either party gives notice of non-renewal. Mr. Nelson is entitled to a minimum annual salary of \$350,000 pursuant to the agreement, as well as annual performance bonuses and participation in the Company's benefit plans. Under the agreement, upon a termination of Mr. Nelson's employment by the Company without cause or by Mr. Nelson for good reason, Mr. Nelson will be entitled to severance payments equal to 200% of the sum of his base salary plus annual

bonus, payable in 24 equal monthly installments following the date of termination, as well as 18 months of continued medical coverage. If such a termination occurs within six months before or two years following a change in control, Mr. Nelson will be entitled to severance payments equal to 300% of the sum of his base salary plus annual bonus, payable in a lump sum, as well as 18 months of continued medical coverage. All of the aforementioned severance benefits are contingent upon Mr. Nelson's execution of a general release of claims. Under the agreement, Mr. Nelson will be subject to 24-month non-compete and non-solicit restrictive covenants following the termination of his employment.

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Termination and Change in Control Benefits under Employment Agreements with Messrs. Gulling, Olafson, and Winterbottom

We entered into new employment agreements with each of Messrs. Gulling, Olafson, and Winterbottom, effective July 23, 2012, which superseded their prior employment agreements in their entirety. Under their respective agreements, Mr. Gulling will serve as Executive Vice President and Chief Financial Officer of the Company and Chief Financial Officer of West Bank, Mr. Olafson will serve as Executive Vice President and Chief Risk Officer of the Company and West Bank, and Mr. Winterbottom will serve as Executive Vice President of the Company and President of West Bank. Each individual will also serve as a member of the board of directors of West Bank. The initial term under each agreement ends on December 31, 2014, but the agreements renew automatically for one-year terms on January 1, 2014, and on each January 1 thereafter unless either party gives notice of non-renewal. Messrs. Gulling, Olafson, and Winterbottom are each entitled to a minimum annual salary of \$247,000 pursuant to their agreements, as well as annual performance bonuses and participation in the Company's benefit plans. Under the agreements, upon a termination of the respective executive's employment by the Company without cause or by the executive for good reason, the executive will be entitled to severance payments equal to 100% of the sum of his base salary plus annual bonus, payable in 12 equal monthly installments following the date of termination, as well as 12 months of continued medical coverage. If such a termination occurs within six months before or two years following a change in control, the executive will be entitled to severance payments equal to 200% of the sum of his base salary plus annual bonus, payable in a lump sum, as well as 18 months of continued medical coverage. All of the aforementioned severance benefits are contingent upon the respective executive's execution of a general release of claims. Under the agreements, Messrs. Gulling, Olafson, and Winterbottom will be subject to 12-month non-compete and non-solicit restrictive covenants following termination of employment (24 months if the termination occurs following a change in control of the Company).

Termination and Change in Control Benefits under 2012 Equity Incentive Plan

All restricted stock units under the 2012 Plan then held by the participant will become fully vested immediately if (1) the 2012 Plan and the respective award agreements are not fully assumed in the change in control or (2) the 2012 Plan and the respective award agreements are fully assumed in the change in control and the participant incurs a termination of service by the Company or a subsidiary without cause or by the participant for good reason.

Further under the 2012 Plan, all restricted stock units generally will become fully vested upon the participant's termination of service due to the participant's disability or the participant's death.

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INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Audit Committee approved McGladrey LLP, an independent registered public accounting firm, as the principal accountant for the Company for the fiscal year ended December 31, 2013. McGladrey LLP will conduct the audit of the Company and its subsidiary for 2013. McGladrey LLP was also the Company's principal accountant and performed the audit in 2012.

A representative from McGladrey LLP will be present at the Annual Meeting. The representative will have the opportunity to make a statement and will be available to respond to appropriate questions from stockholders.

Audit Fees

During the period covering the fiscal years ended December 31, 2012 and 2011, McGladrey LLP and RSM McGladrey, Inc. (through November 30, 2011, RSM McGladrey, Inc. was an affiliate of McGladrey LLP) performed the professional services listed in the following table.

	2012	2011
Audit fees <sup>(1)</sup>	\$248,345	\$240,000
Audit-related fees <sup>(2)</sup>	27,500	25,000
Tax fees <sup>(3)</sup>	12,270	8,105
All other fees <sup>(4)</sup>	2,313	35,424
Total	\$290,428	\$308,529

(1) Audit fees represent fees for professional services provided for the audit of the Company's annual financial statements, review of the Company's quarterly financial statements in connection with the filing of current and periodic reports, FHA compliance audit, and reporting on internal controls in accordance with Section 404 of Sarbanes-Oxley.

(2) Audit-related fees represent the audit of the Company's Employee Savings and Stock Ownership Plan, filing of a registration statement in 2012, and consultation on accounting issues.

(3) Tax fees represent fees for professional services related to tax compliance, which included review of tax returns and tax advice on several accounting issues.

(4) All other fees represent fees for consulting related to software installation.

The Audit Committee considered whether the non-audit services provided to the Company by McGladrey LLP are compatible with maintaining McGladrey LLP's independence and concluded that the independence of McGladrey LLP is not compromised by the provision of such services. The Audit Committee pre-approves all auditing services and permitted non-audit services, including the fees and terms of those services, to be performed for the Company by its independent registered public accounting firm prior to engagement.

GENERAL MATTERS

Certain Relationships and Related Transactions

Certain directors of the Company have direct and indirect material interests in loans made by West Bank. All of the loans were made in West Bank's ordinary course of business, on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable loans with other persons not related to West Bank or the Company, and did not involve more than the normal risk of collectability or present other unfavorable features. None of the loans have been classified as nonaccrual, past due, restructured, or potential problem loans. The Board considered these loans when considering the independence of its directors and determined that such loans did not prevent the relevant directors from being able to serve as independent directors.

The Audit Committee's charter requires the Audit Committee to review and approve all related party transactions that must be disclosed. All transactions between the Company or its subsidiaries and any related person, including loans made by West Bank involving \$120,000 or more, are reviewed to determine whether all material facts of the transaction are known to the Audit Committee, the transaction complies with known legal requirements, and the transaction is fair to the Company and West Bank. The Audit Committee completed the required review of the fiscal year 2012 related party transactions, and all transactions were approved and ratified.

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2014 Stockholder Proposals

Any proposal which a stockholder intends to present at the 2014 annual meeting of stockholders must be received by the Company by November 6, 2013, in order to be eligible for inclusion in the Company's proxy statement and proxy card relating to such meeting, unless the date of the 2014 annual meeting is changed by more than 30 days from April 25, 2014, in which case the proposal must be received a reasonable time before the Company begins to print and send its proxy materials for the 2014 annual meeting. Upon timely receipt of any such proposal, the Company will determine whether to include such proposal in the proxy statement and proxy in accordance with applicable SEC regulations governing stockholder proposals and the solicitation of proxies.

Stockholders wishing to recommend names of individuals for possible nomination to the Board may do so according to the following procedures:

1. Contact Alice A. Jensen, Corporate Secretary, at the address below to obtain the Board Membership Criteria established by the Board.
2. Provide Ms. Jensen with a typewritten recommendation naming the proposed candidate and specifically explaining how the candidate meets the criteria adopted by the Board.
3. Submit the recommendation to Ms. Jensen no later than 120 days prior to the expected mailing date of the proxy (November 6, 2013).
4. Prove the person making the recommendation is a Company stockholder who owns shares with a market value of at least \$2,000 and who has held those shares for at least one year at the time the submission is made.
5. If the person being recommended is aware of the submission, he or she must sign a statement so indicating.
6. If the person being recommended is not aware of the submission, the submitter must explain why.

The written submission must be mailed or hand delivered to:

Ms. Alice A. Jensen  
Corporate Secretary  
West Bancorporation, Inc.  
1601 22<sup>nd</sup> Street  
West Des Moines, Iowa 50266

Stockholder Communications

It is the general policy of the Board that management speaks for the Company. To the extent stockholders wish to communicate with a Company representative, they may do so by contacting Douglas Gulling, Executive Vice President and Chief Financial Officer, 1601 22<sup>nd</sup> Street, West Des Moines, Iowa 50266. Mr. Gulling may be reached by telephone at 515-222-2300 or by email at [dgulling@westbankiowa.com](mailto:dgulling@westbankiowa.com).

The Company has a process for stockholders to send communications to the Board or any of its individual members. Any stockholder wishing to communicate with one or more Board members should address a written communication to Mr. Gulling at one of the addresses noted above. Mr. Gulling will forward all appropriate stockholder communications to the full Board or its individual members as appropriate. Mr. Gulling will generally not forward communications that are primarily commercial in nature or related to an improper or irrelevant topic.

Form 10-K

The Company has included a copy of its annual report on Form 10-K for the year ended December 31, 2012, as filed with the SEC, with this proxy statement. A request for an additional copy should be directed to Alice A. Jensen,

Corporate Secretary, West Bancorporation, Inc., 1601 22<sup>nd</sup> Street, West Des Moines, Iowa 50266 or by calling 515-222-2300. The Company's Form 10-K will also be available on the SEC's website at <http://www.sec.gov>, and through a link at the Investor Relations, SEC Filings section of the Company's website ([www.westbankiowa.com](http://www.westbankiowa.com)).

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Delivery of Documents to Stockholders Sharing an Address

In some instances, only one annual report or proxy statement is being delivered to two or more stockholders who share an address. The Company will promptly deliver additional copies of its proxy statement, summary annual report, and the annual report on Form 10-K to any stockholder who makes such a request. Any stockholder who wishes to receive separate copies of these documents in the future may notify Alice A. Jensen, Corporate Secretary, at 1601 22<sup>nd</sup> Street, West Des Moines, Iowa 50266, or 515-222-2300. Alternatively, any stockholders sharing an address who are receiving multiple copies of these documents may also notify Ms. Jensen to request delivery of only one copy.

By Order of the Board of Directors,

/s/ Alice A. Jensen

Alice A. Jensen  
Secretary  
West Bancorporation, Inc.  
March 6, 2013

West Bancorporation, Inc.  
 Annual Meeting of Stockholders  
 Thursday, April 25, 2013  
 4:00 p.m.  
 1601 22nd Street  
 West Des Moines, Iowa

Voter Control Number

Proxy Number

Account Number Shares

You may vote by:

INTERNET proxy.ilstk.com  SCAN & E-MAIL info@ilstk.com (must sign and date below)  FAX 630.480.0641 (must sign and date below)	May vote until 11:59 p.m. CST one day prior to meeting date. (DO NOT return card if voting by internet)  info@ilstk.com (must sign and date below)  630.480.0641 (must sign and date below)	MAIL  Return in the envelope provided.  (Allow 10 days for mail delivery)	o With the Board of Directors on all Proposals (must sign and date below) OR Against the Board of Directors on all Proposals (must sign and date below) OR Make individual selections below (must sign and date below)
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NUMBER OF PERSONS ATTENDING

WEST BANCORPORATION, INC., WEST DES MOINES, IOWA  
 PROXY FOR ANNUAL MEETING OF STOCKHOLDERS ON APRIL 25, 2013

The undersigned hereby appoints David R. Milligan and David D. Nelson, or either of them, the undersigned's attorneys and proxies, with full power of substitution, to vote all shares of common stock of West Bancorporation, Inc. which the undersigned is entitled to vote as of the record date, February 21, 2013, as fully as the undersigned could do if personally present, at the Annual Meeting of Stockholders of said corporation to be held in the David L. Miller Conference Center at the headquarters of the Company, located at 1601 22nd Street, West Des Moines, Iowa, on Thursday, April 25, 2013, at 4:00 p.m. Central Time, and any and all adjournments thereof.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR PROPOSALS 1, 2, and 3.

		FOR VOTE WITHHELD		FOR VOTE WITHHELD	
1. Election of Directors:	01 Frank W. Berlin	o	o	08 David R. Milligan	o o
	02 Thomas A. Carlstrom	o	o	09 George D. Milligan	o o
	03 Joyce A. Chapman	o	o	10 David D. Nelson	o o
	04 Steven K. Gaer	o	o	11 James W. Noyce	o o
		o	o		o o

05 Michael J.  
Gerdin

12 Robert G.  
Pulver

06 Kaye R. Lozier

13 Lou Ann  
Sandburg

07 Sean P.  
McMurray

14 Philip Jason  
Worth

2. To approve, on a non-binding basis, the 2012 compensation of the named executive officers disclosed in the proxy statement.

FOR  AGAINST  ABSTAIN

3. To ratify the appointment of McGladrey LLP as the Company's independent registered public accounting firm for 2013.

FOR  AGAINST  ABSTAIN

4. In accordance with their discretion, upon all other matters that may properly come before said meeting and any adjournments or postponements thereof.

This proxy, when properly executed, will be voted in the manner directed herein by the undersigned stockholder(s). IF NO DIRECTION IS GIVEN FOR A PARTICULAR MATTER, THIS PROXY WILL BE VOTED (1) FOR THE ELECTION OF THE NOMINEES LISTED IN PROPOSAL 1; (2) FOR THE APPROVAL OF THE COMPENSATION OF THE NAMED EXECUTIVE OFFICERS IN PROPOSAL 2; (3) FOR THE RATIFICATION OF THE APPOINTMENT OF THE INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM IN PROPOSAL 3; AND (4) IN THE DISCRETION OF THE NAMED PROXIES UPON SUCH OTHER MATTERS AS MAY PROPERLY COME BEFORE THE MEETING.

SIGNATURE

DATE

SIGNATURE

DATE

NOTE: PLEASE DATE THE PROXY AND SIGN IT EXACTLY AS THE NAME OR NAMES APPEAR ON THIS CARD. ALL JOINT OWNERS OF SHARES SHOULD SIGN. STATE FULL TITLE WHEN SIGNING AS EXECUTOR, TRUSTEE, GUARDIAN, ETC. PLEASE PROMPTLY RETURN SIGNED PROXY IN THE ENCLOSED ENVELOPE.