

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549**

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**FORM 10-Q**

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**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2014

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

FOR THE TRANSITION PERIOD FROM                      TO  
COMMISSION FILE NUMBER: 0-23599

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**MERCURY SYSTEMS, INC.**

(Exact name of registrant as specified in its charter)

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**MASSACHUSETTS**  
(State or other jurisdiction of  
incorporation or organization)

**04-2741391**  
(I.R.S. Employer  
Identification No.)

**201 RIVERNECK ROAD**  
**CHELMSFORD, MA**  
(Address of principal executive offices)

**01824**  
(Zip Code)

**978-256-1300**  
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 229.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act). Yes  No

Shares of Common Stock outstanding as of October 31, 2014: 33,920,669 shares

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**PART I. FINANCIAL INFORMATION**

**ITEM 1. FINANCIAL STATEMENTS**

**MERCURY SYSTEMS, INC.**  
**CONSOLIDATED BALANCE SHEETS**  
(In thousands, except share and per share data)  
(Unaudited)

	<b>September 30, 2014</b>	<b>June 30, 2014</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 48,876	\$ 47,287
Accounts receivable, net of allowance for doubtful accounts of \$78 and \$34 at September 30, 2014 and June 30, 2014, respectively	35,155	37,625
Unbilled receivables and costs in excess of billings	29,228	22,036
Inventory	30,771	31,655
Deferred income taxes	15,182	15,216
Prepaid income taxes	1,399	1,481
Prepaid expenses and other current assets	4,547	3,631
Current assets of discontinued operations	894	1,374
Total current assets	<u>166,052</u>	<u>160,305</u>
Restricted cash	265	265
Property and equipment, net	13,343	14,144
Goodwill	168,146	168,146
Intangible assets, net	23,244	25,006
Other non-current assets	1,255	987
Non-current assets of discontinued operations	4,685	4,859
Total assets	<u>\$ 376,990</u>	<u>\$ 373,712</u>
<b>Liabilities and Shareholders' Equity</b>		
Current liabilities:		
Accounts payable	\$ 12,384	\$ 7,054
Accrued expenses	9,403	8,377
Accrued compensation	7,265	9,983
Deferred revenues and customer advances	3,649	5,898
Current liabilities of discontinued operations	1,383	1,618
Total current liabilities	<u>34,084</u>	<u>32,930</u>
Deferred gain on sale-leaseback	1,796	2,086
Deferred income taxes	5,437	5,911
Income taxes payable	3,154	3,154
Other non-current liabilities	1,307	1,666
Non-current liabilities of discontinued operations	771	818
Total liabilities	<u>46,549</u>	<u>46,565</u>
Commitments and contingencies (Note 1)		
Shareholders' equity:		
Preferred stock, \$0.01 par value; 1,000,000 shares authorized; no shares issued or outstanding	—	—
Common stock, \$0.01 par value; 85,000,000 shares authorized; 31,981,373 and 31,284,273 shares issued and outstanding at September 30, 2014 and June 30, 2014, respectively	320	312
Additional paid-in capital	244,609	241,725
Retained earnings	84,598	84,099
Accumulated other comprehensive income	914	1,011
Total shareholders' equity	<u>330,441</u>	<u>327,147</u>
Total liabilities and shareholders' equity	<u>\$ 376,990</u>	<u>\$ 373,712</u>

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

**MERCURY SYSTEMS, INC.**  
**CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)**  
(In thousands, except per share data)  
(Unaudited)

	Three Months Ended September 30,	
	2014	2013
Net revenues	\$ 54,061	\$ 50,726
Cost of revenues	30,062	29,164
Gross margin	23,999	21,562
Operating expenses:		
Selling, general and administrative	12,290	14,321
Research and development	7,951	9,312
Amortization of intangible assets	1,762	1,985
Restructuring and other charges	1,268	(15)
Total operating expenses	23,271	25,603
Income (loss) from operations	728	(4,041)
Interest income	3	1
Interest expense	(8)	(15)
Other (expense) income, net	(6)	432
Income (loss) from continuing operations before income taxes	717	(3,623)
Tax benefit	—	(1,319)
Income (loss) from continuing operations	717	(2,304)
(Loss) income from discontinued operations, net of income taxes	(218)	48
Net income (loss)	\$ 499	\$ (2,256)
Basic net earnings (loss) per share:		
Income (loss) from continuing operations	\$ 0.02	\$ (0.07)
(Loss) income from discontinued operations, net of income taxes	—	—
Net income (loss)	\$ 0.02	\$ (0.07)
Diluted net earnings (loss) per share:		
Income (loss) from continuing operations	\$ 0.02	\$ (0.07)
(Loss) income from discontinued operations, net of income taxes	—	—
Net income (loss)	\$ 0.02	\$ (0.07)
Weighted-average shares outstanding:		
Basic	31,635	30,653
Diluted	32,481	30,653
Comprehensive income (loss):		
Net income (loss)	\$ 499	\$ (2,256)
Foreign currency translation adjustments	(97)	59
Total comprehensive income (loss)	\$ 402	\$ (2,197)

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

**MERCURY SYSTEMS, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In thousands)  
(Unaudited)

	Three Months Ended September 30,	
	2014	2013
Cash flows from operating activities:		
Net income (loss)	\$ 499	\$ (2,256)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization expense	3,630	4,120
Stock-based compensation expense	2,614	3,035
(Benefit) provision for deferred income taxes	(820)	464
Excess tax benefit from stock-based compensation	(316)	—
Other non-cash items	(285)	(243)
Changes in operating assets and liabilities:		
Accounts receivable, unbilled receivables, and costs in excess of billings	(4,303)	(731)
Inventory	859	2,274
Prepaid income taxes	83	(1,172)
Prepaid expenses and other current assets	(902)	736
Other non-current assets	146	27
Accounts payable and accrued expenses	3,544	(2,750)
Deferred revenues and customer advances	(2,561)	(1,238)
Other non-current liabilities	(10)	(93)
Net cash provided by operating activities	2,178	2,173
Cash flows from investing activities:		
Purchases of property and equipment	(905)	(1,108)
Net cash used in investing activities	(905)	(1,108)
Cash flows from financing activities:		
Proceeds from employee stock plans	236	60
Excess tax benefits from stock-based compensation	316	—
Payments of capital lease obligations	(160)	(121)
Net cash provided by (used in) financing activities	392	(61)
Effect of exchange rate changes on cash and cash equivalents	(76)	(24)
Net increase in cash and cash equivalents	1,589	980
Cash and cash equivalents at beginning of period	47,287	39,126
Cash and cash equivalents at end of period	\$ 48,876	\$ 40,106
Cash paid during the period for:		
Interest	\$ 8	\$ 15
Income taxes	\$ 374	\$ 334
Supplemental disclosures—non-cash activities:		
Issuance of restricted stock awards to employees	\$ 7,052	\$ 7,728
Capital lease	\$ —	\$ 494

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

## MERCURY SYSTEMS, INC.

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Amounts in thousands except per share data)  
(Unaudited)

#### A. Description of Business

Mercury Systems, Inc. (the "Company" or "Mercury") provides affordable, commercially developed, open sensor processing systems and services for critical commercial, defense and intelligence applications. The Company delivers innovative solutions, rapid time-to-value and service and support to its defense prime contractor customers. The Company's products and solutions have been deployed in more than 300 programs with over 25 different defense prime contractors. Key programs include Aegis, Patriot, Surface Electronic Warfare Improvement Program ("SEWIP"), Gorgon Stare, F-35, Predator and Reaper.

The Company's goal is to grow and build on its position as a critical component of the defense industrial base and become the leading provider of open and affordable sensor processing systems. The Mercury Commercial Electronics ("MCE") operating segment designs, develops and builds open sensor processing products and subsystems that include embedded processing modules and subsystems, radio frequency ("RF") and microwave multi-function assemblies as well as subsystems, and RF and microwave components. The Mercury Defense Systems ("MDS") operating segment provides significant capabilities relating to pre-integrated, open, affordable electronic warfare ("EW"), electronic attack ("EA") and electronic counter measure ("ECM") subsystems and significant capabilities in signals intelligence ("SIGINT") and electro-optical/infrared ("EO/IR") processing technologies.

In June 2014, the Company initiated a plan to divest the Mercury Intelligence Systems ("MIS") operating segment, based on the Company's strategic direction and investment priorities focusing on its core business. As a result, the Company's MIS operating segment met the "held for sale" criteria in accordance with Financial Accounting Standard Boards ("FASB") Accounting Standards Codification ("ASC") 205, *Presentation of Financial Statements*, ("FASB ASC 205") as of June 30, 2014 and all reporting periods thereafter (see Note C to the Consolidated Financial Statements). The consolidated financial statements, excluding the statements of cash flows, and the notes to the consolidated financial statements were restated for all periods presented to reflect the discontinuation of the MIS operating segment, in accordance with FASB ASC 205.

#### B. Summary of Significant Accounting Policies

##### BASIS OF PRESENTATION

The accompanying consolidated financial statements have been prepared by the Company in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") for interim financial information and with the instructions to the Form 10-Q and Article 10 of Regulation S-X. Certain information and footnote disclosures, normally included in annual consolidated financial statements have been condensed or omitted pursuant to those rules and regulations; however, in the opinion of management the financial information reflects all adjustments, consisting of adjustments of a normal recurring nature, necessary for fair presentation. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and related notes for the fiscal year ended June 30, 2014 which are contained in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission ("SEC") on August 14, 2014. The results for the three months ended September 30, 2014 are not necessarily indicative of the results to be expected for the full fiscal year.

The Company is comprised of the following operating segments: MCE and MDS. See Note L of the Notes to Consolidated Financial Statements for further discussion.

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All intercompany transactions and balances have been eliminated in consolidation.

##### USE OF ESTIMATES

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

##### REVENUE RECOGNITION

The Company relies upon FASB ASC 605, *Revenue Recognition* to account for its revenue transactions. Revenue is recognized upon shipment provided that title and risk of loss have passed to the customer, there is persuasive evidence of an arrangement, the sales price is fixed or determinable, collection of the related receivable is reasonably assured, and customer acceptance criteria,

if any, have been successfully demonstrated. Out-of-pocket expenses that are reimbursable by the customer are included in revenue and cost of revenue.

Certain contracts with customers require the Company to perform tests of its products prior to shipment to ensure their performance complies with the Company's published product specifications and, on occasion, with additional customer-requested specifications. In these cases, the Company conducts such tests and, if they are completed successfully, includes a written confirmation with each order shipped. As a result, at the time of each product shipment, the Company believes that no further customer testing requirements exist and that there is no uncertainty of acceptance by its customer.

The Company uses FASB Accounting Standards Update ("ASU") No. 2009-13 ("FASB ASU 2009-13"), *Multiple-Deliverable Revenue Arrangements*. FASB ASU 2009-13 establishes a selling price hierarchy for determining the selling price of a deliverable, which includes: (1) vendor-specific objective evidence ("VSOE") if available; (2) third-party evidence ("TPE") if VSOE is not available; and (3) best estimated selling price ("BESP"), if neither VSOE nor TPE are available. Additionally, FASB ASU 2009-13 expands the disclosure requirements related to a vendor's multiple-deliverable revenue arrangements.

The Company enters into multiple-deliverable arrangements that may include a combination of hardware components, related integration or other services. These arrangements generally do not include any performance-, cancellation-, termination- or refund-type provisions. Total revenue recognized under multiple-deliverable revenue arrangements was 29% of total revenues in the three months ended September 30, 2014 and 2013.

In accordance with the provisions of FASB ASU 2009-13, the Company allocates arrangement consideration to each deliverable in an arrangement based on its relative selling price. The Company generally expects that it will not be able to establish VSOE or TPE due to limited single element transactions and the nature of the markets in which the Company competes, and, as such, the Company typically determines its relative selling price using BESP.

The objective of BESP is to determine the price at which the Company would transact if the product or service were sold by the Company on a standalone basis. Determination of BESP involves the consideration of several factors based on the specific facts and circumstances of each arrangement. Specifically, the Company considers the cost to produce the deliverable, the anticipated margin on that deliverable, the selling price and profit margin for similar parts, the Company's ongoing pricing strategy and policies as evident from the price list established and updated by management on a regular basis, the value of any enhancements that have been built into the deliverable and the characteristics of the varying markets in which the deliverable is sold.

The Company analyzes the selling prices used in its allocation of arrangement consideration at a minimum on an annual basis and on a more frequent basis if a significant change in the Company's business necessitates a more timely analysis or if the Company experiences significant variances in its selling prices.

Each deliverable within the Company's multiple-deliverable revenue arrangements is accounted for as a separate unit of accounting under the guidance of FASB ASU 2009-13 if both of the following criteria are met: the delivered item or items have value to the customer on a standalone basis; and for an arrangement that includes a general right of return relative to the delivered item(s), delivery or performance of the undelivered item(s) is considered probable and substantially in the control of the Company. The Company's revenue arrangements generally do not include a general right of return for delivered products. The Company considers a deliverable to have standalone value if the item is sold separately by the Company or another vendor or if the item could be resold by the customer.

Deliverables not meeting the criteria for being a separate unit of accounting are combined with a deliverable that does meet that criterion. The appropriate allocation of arrangement consideration and recognition of revenue is then determined for the combined unit of accounting.

The Company also engages in long-term contracts for development, production and services activities which it accounts for consistent with FASB ASC 605-35, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts*, and other relevant revenue recognition accounting literature. The Company considers the nature of these contracts and the types of products and services provided when determining the proper accounting for a particular contract. Generally for fixed-price contracts, other than service-type contracts, revenue is recognized primarily under the percentage of completion method or, for certain short-term contracts, by the completed contract method. Revenue from service-type fixed-price contracts is recognized ratably over the contract period or by other appropriate input or output methods to measure service provided, and contract costs are expensed as incurred. The Company establishes billing terms at the time project deliverables and milestones are agreed. Revenues recognized in excess of the amounts invoiced to clients are classified as unbilled receivables. For time and materials contracts, revenue reflects the number of direct labor hours expended in the performance of a contract multiplied by the contract billing rate, as well as reimbursement of other billable direct costs. For all types of contracts, the Company recognizes anticipated contract losses as soon as they become known and estimable.

The use of contract accounting requires significant judgment relative to estimating total contract revenues and costs, including assumptions relative to the length of time to complete the contract, the nature and complexity of the work to be performed, anticipated increases in wages and prices for subcontractor services and materials, and the availability of subcontractor services

and materials. The Company's estimates are based upon the professional knowledge and experience of its engineers, program managers and other personnel, who review each long-term contract monthly to assess the contract's schedule, performance, technical matters and estimated cost at completion. Changes in estimates are applied retrospectively and when adjustments in estimated contract costs are identified, such revisions may result in current period adjustments to earnings applicable to performance in prior periods.

The Company defines service revenues as revenue from activities that are not associated with the design, development, production, or delivery of tangible assets, software or specific capabilities sold by us. Examples of the Company's service revenues include: analyst services and systems engineering support, consulting, maintenance and other support, testing and installation. The Company combines its product and service revenues into a single class as services revenues do not exceed 10 percent of total revenues.

The Company does not provide its customers with rights of product return, other than those related to warranty provisions that permit repair or replacement of defective goods. The Company accrues for anticipated warranty costs upon product shipment. Revenues from product royalties are recognized upon invoice by the Company. Additionally, all revenues are reported net of government assessed taxes (e.g. sales taxes or value-added taxes).

#### WEIGHTED-AVERAGE SHARES

Weighted-average shares were calculated as follows:

	<b>Three Months Ended September 30,</b>	
	<b>2014</b>	<b>2013</b>
Basic weighted-average shares outstanding	31,635	30,653
Effect of dilutive equity instruments	846	—
Diluted weighted-average shares outstanding	<u>32,481</u>	<u>30,653</u>

Equity instruments to purchase 750 and 4,178 shares of common stock were not included in the calculation of diluted net earnings per share for the three months ended September 30, 2014 and 2013, respectively, because the equity instruments were anti-dilutive.

#### C. Discontinued Operations

During the fourth quarter of fiscal 2014, the Company conducted a strategic review of the Mercury Intelligence Systems ("MIS") business unit which encompassed an assessment of MIS' financial performance and contemporaneous future financial projections. The Company, with Board of Director's approval, concluded that a plan to divest the MIS business unit would be in the best interests of the Company and its shareholders.

The Company's MIS business unit met the "held for sale" criteria in accordance with FASB ASC 205. As the Company does not anticipate continuing involvement in the operations of MIS after its divestiture, the MIS operating results have been reported as a discontinued operation for all periods presented.

MIS is considered its own operating segment and was previously aggregated with MDS into one reportable segment based on similar economic and qualitative factors in accordance with FASB ASC 280. As MIS is a discontinued operation, the results of MIS have been excluded from the MDS reportable segment. Accordingly, the revenues, costs of revenue, operating expenses, assets and liabilities of MIS have been reported separately in the Consolidated Statements of Operations and Comprehensive Income (Loss) and Consolidated Balance Sheets for all periods presented. The discontinued operation's balances in the Consolidated Balance Sheets do not reflect intercompany receivable balances of MIS, and the results of discontinued operations do not reflect interest expense or the allocation of the Company's corporate general and administrative expenses.



The amounts reported in (loss) income from discontinued operations, net of income taxes were as follows:

	For the Three Months Ended September 30,	
	2014	2013
Net revenues of discontinued operations	\$ 1,839	\$ 3,214
Costs of discontinued operations:		
Cost of revenues	1,225	2,191
Selling, general and administrative	647	780
Research and development	171	32
Amortization of intangible assets	124	123
Acquisition costs and other related expenses	33	—
(Loss) income from discontinued operations before income taxes	(361)	88
Tax (benefit) provision	(143)	40
(Loss) income from discontinued operations	\$ (218)	\$ 48

The amounts reported as assets and liabilities of the discontinued operations were as follows:

	September 30, 2014	June 30, 2014
Accounts receivable, net	\$ 303	\$ 925
Unbilled receivables and costs in excess of billings	401	248
Deferred income taxes	88	77
Prepaid expenses and other current assets	102	124
Property and equipment, net	431	475
Goodwill	2,283	2,283
Intangible assets, net	1,938	2,062
Other non-current assets	33	39
Assets of discontinued operations	\$ 5,579	\$ 6,233
Accounts payable	\$ 21	\$ 127
Accrued expenses	879	802
Accrued compensation	483	689
Deferred income taxes	771	818
Liabilities of discontinued operations	\$ 2,154	\$ 2,436

The depreciation, amortization and significant operating and investing non-cash items of the discontinued operations were as follows:

	For the Three Months Ended September 30,	
	2014	2013
Depreciation	\$ 44	\$ 38
Amortization of intangible assets	\$ 124	\$ 123
Stock-based compensation expense	\$ 63	\$ 47

#### D. Fair Value of Financial Instruments

The Company measures at fair value certain financial assets and liabilities, including cash equivalents and restricted cash. FASB ASC 820, *Fair Value Measurement and Disclosures*, specifies a hierarchy of valuation techniques based on whether the

inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. These two types of inputs have created the following fair-value hierarchy:

Level 1—Quoted prices for identical instruments in active markets;

Level 2—Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets; and

Level 3—Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable.

The following table summarizes the Company's financial assets measured at fair value on a recurring basis at September 30, 2014:

	Fair Value Measurements			
	September 30, 2014	Level 1	Level 2	Level 3
Assets:				
Cash and cash equivalents	\$ 48,876	\$ 48,876	\$ —	\$ —
Restricted cash	265	265	—	—
Total	\$ 49,141	\$ 49,141	\$ —	\$ —

The carrying values of cash and cash equivalents, including all U.S. Treasury Bills and money market funds, accounts receivable and payable, and accrued liabilities approximate fair value due to the short-term maturities of these assets and liabilities.

#### E. Inventory

Inventory is stated at the lower of cost (first-in, first-out) or market value, and consists of materials, labor and overhead. On a quarterly basis, the Company uses consistent methodologies to evaluate inventory for net realizable value. Once an item is written down, the value becomes the new inventory cost basis. The Company reduces the value of inventory for excess and obsolete inventory, consisting of on-hand and non-cancelable on-order inventory in excess of estimated usage. The excess and obsolete inventory evaluation is based upon assumptions about future demand, history, product mix and possible alternative uses. Inventory was comprised of the following:

	September 30, 2014	June 30, 2014
Raw materials	\$ 12,845	\$ 13,755
Work in process	14,324	12,677
Finished goods	3,602	5,223
Total	\$ 30,771	\$ 31,655

There are no amounts in inventory relating to contracts having production cycles longer than one year.

#### F. Goodwill

The following table sets forth the carrying amount of goodwill by reporting units as of September 30, 2014 and June 30, 2014:

	September 30, 2014	June 30, 2014
MCE goodwill	\$ 134,378	\$ 134,378
MDS goodwill	33,768	33,768
Total goodwill	\$ 168,146	\$ 168,146

In the three months ended September 30, 2014, there were no triggering events, as defined by FASB ASC 350, which required an interim goodwill impairment test. The Company performs its annual goodwill impairment test in the fourth quarter of each fiscal year.

The Company determines its reporting units in accordance with FASB ASC 350, by assessing whether discrete financial information is available and if management regularly reviews the operating results of that component. Following this assessment, the Company determined that its reporting units are the same as its operating segments, MCE and MDS.

#### G. Restructuring Plan

During fiscal 2014 the Company announced a restructuring plan (“2014 Plan”) that was implemented as part of the final phase of integration activities relating to the Company’s recent acquisitions. The integration plan includes the consolidation of manufacturing facilities, centralization of administrative functions using common information systems and processes, and realignment of research and development resources. During the three months ended September 30, 2014, the Company incurred restructuring and other charges of \$1,268. These charges were primarily associated with the second phase of the Chelmsford, Massachusetts headquarters consolidation and severance costs. Future restructuring expenses associated with the integration plan are expected to be approximately \$1,114, and the actions resulting in those changes are expected to be completed by the second quarter of fiscal 2015. In the event that the Company is unable to sublease the unoccupied portion of its headquarters complex in Chelmsford, MA, it will incur nominal, periodic restructuring charges through fiscal 2017. These restructuring and other charges affect both the MCE and MDS reportable segments.

The following table presents the detail of activity for the Company’s restructuring plans:

	Severance & Related	Facilities & Other	Total
Restructuring liability at June 30, 2014	\$ 1,371	\$ 772	\$ 2,143
MCE restructuring and other charges	669	750	1,419
MDS restructuring and other charges	33	—	33
Cash paid	(962)	(242)	(1,204)
Reversals(*)	(184)	—	(184)
Restructuring liability at September 30, 2014	<u>\$ 927</u>	<u>\$ 1,280</u>	<u>\$ 2,207</u>

(\*) Reversals result from the finalization of settlements owed.

All of the restructuring and other charges are classified as operating expenses in the consolidated statements of operations and comprehensive income (loss) and any remaining obligations are expected to be paid within the next twelve months. The restructuring liability is classified as accrued expenses in the consolidated balance sheets.

#### H. Income Taxes

The Company recorded a tax benefit of \$0 and \$1,319 on an income before income taxes of \$717 and a loss before income taxes of \$3,623 for the three months ended September 30, 2014 and 2013, respectively. Income tax benefit for the three months ended September 30, 2014 differed from the federal statutory rate primarily due to the impact of Section 199 manufacturing deduction, stock compensation and state taxes. Income tax benefit for the three months ended September 30, 2013 differed from the federal statutory rate primarily due to the impact of federal research and development tax credits, Section 199 manufacturing deduction and stock compensation.

No material changes in the Company’s unrecognized tax positions occurred during the three months ended September 30, 2014. The Company estimates that unrecognized tax benefits of up to \$1,022 could be realized within the next 12 months as a result of resolutions of tax positions and the expiration of applicable statutes of limitations.

#### I. Commitments and Contingencies

##### LEGAL CLAIMS

The Company is subject to litigation, claims, investigations and audits arising from time to time in the ordinary course of our business. Although legal proceedings are inherently unpredictable, the Company believes that it has valid defenses with respect to any matters currently pending against the Company and intends to defend itself vigorously. The outcome of these matters, individually and in the aggregate, is not expected to have a material impact on the Company’s cash flows, results of operations, or financial position.

##### INDEMNIFICATION OBLIGATIONS

The Company’s standard product sales and license agreements entered into in the ordinary course of business typically contain an indemnification provision pursuant to which the Company indemnifies, holds harmless, and agrees to reimburse the

indemnified party for losses suffered or incurred by the indemnified party in connection with any patent, copyright or other intellectual property infringement claim by any third party with respect to the Company's products. Such provisions generally survive termination or expiration of the agreements. The potential amount of future payments the Company could be required to make under these indemnification provisions is, in some instances, unlimited.

#### PURCHASE COMMITMENTS

As of September 30, 2014, the Company has entered into non-cancelable purchase commitments for certain inventory components and services used in its normal operations. The purchase commitments covered by these agreements are for less than one year and aggregate to \$31,118.

#### **J. Debt**

##### *Senior Unsecured Credit Facility*

As of September 30, 2014, there was \$86,557 of borrowing capacity available under the Company's credit agreement with a syndicate of commercial banks, with Key Bank National Association acting as the administrative agent. The Company can borrow up to \$200,000 based on the Company's consolidated EBITDA for the trailing four quarters. There were no borrowings outstanding on the credit agreement; however, there were outstanding letters of credit of \$3,789. The Company was in compliance with all covenants and conditions under the credit agreement.

#### **K. Stock-Based Compensation**

##### STOCK OPTION PLANS

The number of shares authorized for issuance under the Company's 2005 Stock Incentive Plan, as amended and restated (the "2005 Plan"), is 8,018 shares at September 30, 2014. The 2005 Plan will be increased by any future cancellations, forfeitures or terminations (other than by exercise) under the 1997 Plan. The 2005 Plan provides for the grant of non-qualified and incentive stock options, restricted stock, stock appreciation rights and deferred stock awards to employees and non-employees. All stock options are granted with an exercise price of not less than 100% of the fair value of the Company's common stock at the date of grant and the options generally have a term of seven years. There were 567 shares available for future grant under the 2005 Plan at September 30, 2014. Subsequent to September 30, 2014, the Company's shareholders approved an increase of 3,200 shares.

On August 15, 2014, as part of the Company's ongoing annual equity grant program for employees, the Company granted for the first time performance-based restricted stock awards to certain executives pursuant to the 2005 Plan. These performance awards vest annually over a three year requisite service period subject to the achievement of specific performance targets related to adjusted EBITDA as a percentage of revenue. Based on the performance targets, these awards require graded vesting that results in more rapid expense recognition compared to traditional time-based vesting over the same vesting period. The Company will monitor the probability of achieving the performance targets on a quarterly basis and may adjust periodic compensation expense accordingly.

##### EMPLOYEE STOCK PURCHASE PLAN

The number of shares authorized for issuance under the Company's 1997 Employee Stock Purchase Plan, as amended and restated ("ESPP"), is 1,400 shares. Under the ESPP, rights are granted to purchase shares of common stock at 85% of the lesser of the market value of such shares at either the beginning or the end of each six-month offering period. The ESPP permits employees to purchase common stock through payroll deductions, which may not exceed 10% of an employee's compensation as defined in the ESPP. There were no shares issued under the ESPP during the three months ended September 30, 2014 and 2013, respectively. Shares available for future purchase under the ESPP totaled 164 at September 30, 2014.

STOCK OPTION AND AWARD ACTIVITY

The following table summarizes activity of the Company's stock option plans since June 30, 2014:

	Options Outstanding		
	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)
<b>Outstanding at June 30, 2014</b>	<b>1,435</b>	<b>\$ 11.76</b>	<b>2.23</b>
Granted	—	—	
Exercised	(37)	6.33	
Cancelled	(62)	23.58	
<b>Outstanding at September 30, 2014</b>	<b>1,336</b>	<b>\$ 11.37</b>	<b>2.02</b>

The following table summarizes the status of the Company's non-vested restricted stock awards since June 30, 2014:

	Non-vested Restricted Stock Awards	
	Number of Shares	Weighted Average Grant Date Fair Value
<b>Outstanding at June 30, 2014</b>	<b>2,091</b>	<b>\$ 10.15</b>
Granted	620	11.38
Vested	(660)	10.31
Forfeited	(126)	10.90
<b>Outstanding at September 30, 2014</b>	<b>1,925</b>	<b>\$ 10.44</b>

STOCK-BASED COMPENSATION EXPENSE

The Company recognized the full expense of its share-based payment plans in the consolidated statements of operations for the three months ended September 30, 2014 and 2013 in accordance with FASB ASC 718 and did not capitalize any such costs on the consolidated balance sheets, as such costs that qualified for capitalization were not material. Under the fair value recognition provisions of FASB ASC 718, stock-based compensation cost is measured at the grant date based on the value of the award and is recognized as expense over the service period, net of estimated forfeitures. The following table presents share-based compensation expenses included in the Company's consolidated statements of operations:

	Three Months Ended September 30,	
	2014	2013
Cost of revenues	\$ 151	\$ 207
Selling, general and administrative	1,966	2,314
Research and development	434	467
Share-based compensation expense before tax	2,551	2,988
Income tax benefit	(919)	(1,072)
Net compensation expense	<u>\$ 1,632</u>	<u>\$ 1,916</u>

**L. Operating Segment, Geographic Information and Significant Customers**

Operating segments are defined as components of an enterprise evaluated regularly by the Company's chief operating decision maker ("CODM") in deciding how to allocate resources and assess performance. The Company utilizes the management approach for determining reportable segments in accordance with the authoritative guidance. The following operating segments were determined based upon the nature of the products offered to customers, the market characteristics of each operating segment and the Company's management structure:

- Mercury Commercial Electronics ("MCE"): this operating segment delivers affordable, innovative, commercially developed, specialized processing subsystems for critical commercial, defense and intelligence applications. MCE delivers secure solutions that are based upon open architectures and widely adopted industry standards. MCE delivers

rapid time-to-value and service and support to prime defense contractors and commercial customers. MCE provides solutions to prime contractor customers on a variety of programs. MCE also provides technology building blocks to Mercury Defense Systems on key classified and unclassified programs. MCE has a legacy of embedded multi-computing and embedded sensor processing expertise. More recently, MCE has added substantial capabilities around radio frequency ("RF") and microwave technologies as well as emerging new manufacturing capabilities to bring design, production and test capabilities of its RF and microwave solutions to market on a more scalable basis.

- Mercury Defense Systems ("MDS"): this operating segment provides significant capabilities relating to pre-integrated, open, affordable electronic warfare ("EW"), electronic attack ("EA") and electronic counter measure ("ECM") subsystems, and signals intelligence ("SIGINT") and electro-optical/infrared ("EO/IR") processing technologies. MDS deploys these solutions on behalf of defense prime contractors and the Department of Defense ("DoD"), leveraging commercially available technologies and solutions (or "building blocks") from the MCE business and other commercial suppliers. MDS leverages this technology to develop integrated sensor processing subsystems, often including classified application-specific software and intellectual property ("IP") for the C4ISR (command, control, communications, computers, intelligence, surveillance and reconnaissance), EW, and ECM markets. MDS brings significant domain expertise to customers, drawing on over 25 years of experience in EW, SIGINT, and radar environment test and simulation.

The Company's operating segments were evaluated in accordance with FASB ASC 280 "*Segment Reporting*" in order to determine which operating segments qualified as reportable segments. The Company determined that both MCE and MDS met the quantitative thresholds for reporting.

Prior year results have been restated for the reclassification of the MIS operating segment as discontinued operations. MIS was previously aggregated with MDS into one reportable segment based on similar economic and qualitative factors in accordance with FASB ASC 280 (see Note C).

The accounting policies of the reportable segments are the same as those described in "Note B: Summary of Significant Accounting Policies." The profitability measure employed by the Company and its CODM as the basis for allocating resources to segments and assessing segment performance is adjusted EBITDA. The Company believes the adjusted EBITDA financial measure assists in providing an enhanced understanding of its underlying operational measures to manage its business, to evaluate its performance compared to prior periods and the marketplace, and to establish operational goals.

Adjusted EBITDA is defined as income from continuing operations before interest income and expense, income taxes, depreciation, amortization of intangible assets, restructuring and other charges, impairment of long-lived assets, acquisition costs and other related expenses, fair value adjustments from purchase accounting and stock-based compensation costs. Additionally, asset information by reportable segment is not reported because the Company and its CODM utilize consolidated asset information when making business decisions. The following is a summary of the performance of the Company's operations by reportable segment:

	MCE	MDS	Eliminations	Total
<b>THREE MONTHS ENDED</b>				
<b>SEPTEMBER 30, 2014</b>				
Net revenues to unaffiliated customers	\$ 48,556	\$ 5,379	\$ 126	\$ 54,061
Intersegment revenues	501	140	(641)	—
Net revenues	<u>\$ 49,057</u>	<u>\$ 5,519</u>	<u>\$ (515)</u>	<u>\$ 54,061</u>
Adjusted EBITDA	<u>\$ 7,289</u>	<u>\$ 486</u>	<u>\$ 228</u>	<u>\$ 8,003</u>
<b>THREE MONTHS ENDED</b>				
<b>SEPTEMBER 30, 2013</b>				
Net revenues to unaffiliated customers	\$ 43,488	\$ 7,916	\$ (678)	\$ 50,726
Intersegment revenues	1,114	—	(1,114)	—
Net revenues	<u>\$ 44,602</u>	<u>\$ 7,916</u>	<u>\$ (1,792)</u>	<u>\$ 50,726</u>
Adjusted EBITDA	<u>\$ 2,343</u>	<u>\$ 1,062</u>	<u>\$ (82)</u>	<u>\$ 3,323</u>

The following table reconciles the Company's income (loss) from continuing operations, the most directly comparable GAAP financial measure, to its adjusted EBITDA:

	Three Months Ended September 30,	
	2014	2013
Income (loss) from continuing operations	\$ 717	\$ (2,304)
Interest expense, net	5	14
Tax benefit	—	(1,319)
Depreciation	1,700	1,974
Amortization of intangible assets	1,762	1,985
Restructuring and other charges	1,268	(15)
Stock-based compensation expense	2,551	2,988
Adjusted EBITDA	<u>\$ 8,003</u>	<u>\$ 3,323</u>

The geographic distribution of the Company's revenues is summarized as follows:

	US	Europe	Asia Pacific	Eliminations	Total
<b>THREE MONTHS ENDED SEPTEMBER 30, 2014</b>					
Net revenues to unaffiliated customers	\$ 53,085	\$ 346	\$ 630	\$ —	\$ 54,061
Inter-geographic revenues	583	—	—	(583)	—
Net revenues	<u>\$ 53,668</u>	<u>\$ 346</u>	<u>\$ 630</u>	<u>\$ (583)</u>	<u>\$ 54,061</u>
<b>THREE MONTHS ENDED SEPTEMBER 30, 2013</b>					
Net revenues to unaffiliated customers	\$ 49,456	\$ 508	\$ 762	\$ —	\$ 50,726
Inter-geographic revenues	819	157	140	(1,116)	—
Net revenues	<u>\$ 50,275</u>	<u>\$ 665</u>	<u>\$ 902</u>	<u>\$ (1,116)</u>	<u>\$ 50,726</u>

Foreign revenue is based on the country in which the Company's legal subsidiary is domiciled.

The geographic distribution of the Company's long-lived assets is summarized as follows:

	U.S.	Europe	Asia Pacific	Eliminations	Total
September 30, 2014	\$ 13,298	\$ 40	\$ 5	\$ —	\$ 13,343
June 30, 2014	\$ 14,090	\$ 48	\$ 6	\$ —	\$ 14,144

Identifiable long-lived assets exclude goodwill and intangible assets.

Customers comprising 10% or more of the Company's revenues for the periods shown below are as follows:

	Three Months Ended September 30,	
	2014	2013
Raytheon Company	35%	13%
Lockheed Martin Corporation	30%	12%
Northrop Grumman Corporation	*	16%
BAE Systems PLC	*	11%
	<u>65%</u>	<u>52%</u>

\* Indicates that the amount is less than 10% of the Company's revenues for the respective period.

While the Company typically has customers from which it derives 10% or more of its revenue, the sales to each of these customers are spread across multiple programs and platforms. Programs comprising 10% or more of the Company's revenues for the periods shown below are as follows:

	Three Months Ended September 30,	
	2014	2013
SEWIP	18%	*
Patriot	18%	*
Aegis	11%	*
F-35	10%	*
	57%	—%

\* Indicates that the amount is less than 10% of the Company's revenues for the respective period.

**M. Subsequent Events**

The Company has evaluated subsequent events from the date of the consolidated balance sheet through the date the consolidated financial statements were issued.



## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

### FORWARD-LOOKING STATEMENTS

From time to time, information provided, statements made by our employees or information included in our filings with the Securities and Exchange Commission may contain statements that are not historical facts but that are "forward-looking statements," which involve risks and uncertainties. You can identify these statements by the use of the words "may," "will," "could," "should," "would," "plans," "expects," "anticipates," "continue," "estimate," "project," "intend," "likely," "forecast," "probable," "potential," and similar expressions. These forward-looking statements involve risks and uncertainties that could cause actual results to differ materially from those projected or anticipated. Such risks and uncertainties include, but are not limited to, continued funding of defense programs, the timing and amounts of such funding, general economic and business conditions, including unforeseen weakness in the Company's markets, effects of continued geopolitical unrest and regional conflicts, competition, changes in technology and methods of marketing, delays in completing engineering and manufacturing programs, changes in customer order patterns, changes in product mix, continued success in technological advances and delivering technological innovations, changes in, or in the U.S. Government's interpretation of, federal export control or procurement rules and regulations, market acceptance of the Company's products, shortages in components, production delays due to performance quality issues with outsourced components, inability to fully realize the expected benefits from acquisitions, divestitures and restructurings, or delays in realizing such benefits, challenges in integrating acquired businesses and achieving anticipated synergies, changes to export regulations, increases in tax rates, changes to generally accepted accounting principles, difficulties in retaining key employees and customers, unanticipated costs under fixed-price service and system integration engagements, and various other factors beyond our control. These risks and uncertainties also include such additional risk factors as set forth under Part I-Item 1A (Risk Factors) in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2014. We caution readers not to place undue reliance upon any such forward-looking statements, which speak only as of the date made. We undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made.

### OVERVIEW

Mercury Systems provides affordable, commercially developed, open sensor processing systems and services for critical commercial, defense, and intelligence applications. We deliver innovative solutions, rapid time-to-value and service and support to our defense prime contractor customers. Our products and solutions have been deployed in more than 300 programs with over 25 different defense prime contractors. Key programs include Aegis, Patriot, Surface Electronic Warfare Improvement Program ("SEWIP"), Gorgon Stare, Predator, F-35 and Reaper. Our organizational structure allows the Company to deliver capabilities that combine technology building blocks and deep domain expertise in the defense sector. We believe our total portfolio of services and solutions is unique in the industry for a commercial company. Mercury Systems operates across a broad spectrum of defense programs and, effective for fiscal 2015, we deliver our solutions and services via two business units: (i) Mercury Commercial Electronics; and (ii) Mercury Defense Systems. In the fourth quarter of fiscal 2014, we initiated a plan to divest our Mercury Intelligence Systems business unit. Consequently, its operating results are included in discontinued operations for all periods presented (see Note C to the consolidated financial statements).

As of September 30, 2014, we had 625 employees. Our revenue, income from continuing operations and adjusted EBITDA for the three month period ended September 30, 2014 were \$54.1 million, \$0.7 million, and \$8.0 million, respectively. See the Non-GAAP Financial Measures section for a reconciliation of our income (loss) from continuing operations to adjusted EBITDA.

Our operations are organized in the following two reportable segments: (i) Mercury Commercial Electronics ("MCE") and (ii) Mercury Defense Systems ("MDS").

*Mercury Commercial Electronics*, or MCE, provides affordable, innovative, commercially designed and developed, specialized processing subsystems for critical commercial, defense and intelligence applications. We deliver innovative solutions, rapid time-to-value and service and support to our prime defense contractor customers. Our technologies and capabilities include embedded processing modules and subsystems, RF and microwave multi-function assemblies as well as subsystems, and RF and microwave components.

MCE utilizes leading edge, high performance computing technologies architected by leveraging open standards and open architectures to address highly data-intensive applications that include signal, sensor and image processing; all of this while addressing the packaging challenges, often referred to as "SWaP" (size, weight, and power) that are common in military as well as some commercial applications. In addition, MCE designs and builds RF and microwave components and subsystems to meet the needs of the electronic warfare ("EW"), signals intelligence ("SIGINT") and other high bandwidth communications requirements and applications.

For the three months ended September 30, 2014, MCE accounted for approximately 90% of our total net revenues.

*Mercury Defense Systems*, or MDS, provides significant capabilities relating to pre-integrated, open, affordable EW, electronic attack ("EA") and electronic counter measure ("ECM") subsystems, and SIGINT and electro-optical/infrared ("EO/IR") processing technologies. MDS deploys these solutions on behalf of defense prime contractors and the Department of Defense ("DoD"), leveraging commercially available technologies and solutions (or "building blocks") from our MCE business and other commercial suppliers. MDS leverages this technology to develop integrated sensor processing subsystems, often including classified application-specific software and intellectual property ("IP") for the C4ISR (command, control, communications, computers, intelligence, surveillance and reconnaissance), EW, and ECM markets. MDS brings significant domain expertise to customers, drawing on over 25 years of experience in EW, SIGINT, and radar environment test and simulation.

For the three months ended September 30, 2014, MDS accounted for approximately 10% of our total net revenues.

Since we are an OEM supplier to our commercial markets and conduct much of our business with our defense customers via commercial items, requests by customers are a primary driver of revenue fluctuations from quarter to quarter. Customers specify delivery date requirements that coincide with their need for our products. Because these customers may use our products in connection with a variety of defense programs or other projects of different sizes and durations, a customer's orders for one quarter generally do not indicate a trend for future orders by that customer. Additionally, order patterns do not necessarily correlate amongst customers and, therefore, we generally cannot identify sequential quarterly trends, even within our business units.

## RESULTS OF OPERATIONS:

### Three months ended September 30, 2014 compared to the three months ended September 30, 2013

The following tables set forth, for the three months periods indicated, financial data from the consolidated statements of operations:

<u>(In thousands)</u>	<u>September 30, 2014</u>	<u>As a % of Total Net Revenue</u>	<u>September 30, 2013</u>	<u>As a % of Total Net Revenue</u>
Net revenues	\$ 54,061	100.0 %	\$ 50,726	100.0 %
Cost of revenues	30,062	55.6	29,164	57.5
Gross margin	23,999	44.4	21,562	42.5
Operating expenses:				
Selling, general and administrative	12,290	22.7	14,321	28.2
Research and development	7,951	14.7	9,312	18.4
Amortization of intangible assets	1,762	3.3	1,985	3.9
Restructuring and other charges	1,268	2.4	(15)	—
Total operating expenses	23,271	43.1	25,603	50.5
Income (loss) from operations	728	1.3	(4,041)	(8.0)
Other (expense) income, net	(11)	0.0	418	0.9
Income (loss) from continuing operations before income taxes	717	1.3	(3,623)	(7.1)
Tax benefit	—	—	(1,319)	(2.6)
Income (loss) from continuing operations	717	1.3	(2,304)	(4.5)
(Loss) income from discontinued operations, net of taxes	(218)	(0.4)	48	0.1
Net income (loss)	\$ 499	0.9 %	\$ (2,256)	(4.4)%

## REVENUES

<u>(In thousands)</u>	<u>September 30, 2014</u>	<u>September 30, 2013</u>	<u>\$ Change</u>	<u>% Change</u>
MCE	\$ 48,556	\$ 43,488	\$ 5,068	12 %
MDS	5,379	7,916	(2,537)	(32)%
Eliminations	126	(678)	804	119 %
Total revenues	\$ 54,061	\$ 50,726	\$ 3,335	7 %

Total revenues increased \$3.3 million, or 7%, to \$54.1 million during the three months ended September 30, 2014 as compared to the comparable period in fiscal 2014. This increase was driven by higher defense sales of \$8.1 million, partially offset by lower

commercial sales of \$4.8 million. The increase in total revenues is primarily attributed to higher revenues from the Patriot, Aegis, SEWIP, and F-35 programs. International revenues, which consist of foreign military sales through prime defense contractor customers and direct sales to non-U.S. based customers, decreased \$5.0 million to \$10.4 million during the three months ended September 30, 2014, compared to \$15.4 million in the same period in the prior fiscal year. The decrease was primarily driven by lower revenues in the Asia Pacific region. International revenues represented 19% and 30% of total revenues during the three months ended September 30, 2014 and 2013, respectively.

Net MCE revenues increased \$5.1 million, or 12%, during the three months ended September 30, 2014 as compared to the same period in the prior fiscal year. This increase was primarily driven by higher defense sales of \$9.9 million related to increases from the Patriot, Aegis, SEWIP, and F-35 programs, partially offset by lower foreign military sales and a \$4.8 million decrease in commercial sales.

Net MDS revenues decreased \$2.5 million, or 32%, during the three months ended September 30, 2014 as compared to the same period in the previous fiscal year. This decrease was primarily driven by lower revenues related to radar environment test and simulation sales.

Eliminations revenue is attributable to development programs where the revenue is recognized in each segment under contract accounting, and reflects the reconciliation to our consolidated results.

#### GROSS MARGIN

Gross margin was 44.4% for the three months ended September 30, 2014, an increase of 190 basis points from the 42.5% gross margin achieved during the same period in fiscal 2014. The higher gross margin between years was due to a more favorable product mix, primarily driven by a recovery in our higher margin digital signal processing business within MCE and facilities consolidations as part of our integration plan.

#### SELLING, GENERAL AND ADMINISTRATIVE

Selling, general and administrative expenses decreased \$2.0 million, or 14%, to \$12.3 million during the three months ended September 30, 2014, compared to \$14.3 million during the comparable period in fiscal 2014. The decrease was primarily due to lower employee compensation expenses as a result of progress achieved on our plan of integrating and consolidating facilities, systems, and processes. Selling, general and administrative expenses decreased as a percentage of revenues to 22.7% during the three months ended September 30, 2014 from 28.2% during the same period in fiscal 2014 due to higher revenues in the first quarter of fiscal 2015 and overall expense reductions, as compared to the comparable period in fiscal 2014.

#### RESEARCH AND DEVELOPMENT

Research and development expenses decreased \$1.3 million, or 15%, to \$8.0 million during the three months ended September 30, 2014, compared to \$9.3 million during the comparable period in fiscal 2014. The decrease was primarily due to higher customer funded development and lower headcount between years.

#### AMORTIZATION OF INTANGIBLE ASSETS

Amortization of intangible assets decreased \$0.2 million, or 11%, to \$1.8 million for the three months ended September 30, 2014 as compared to \$2.0 million during the comparable period in fiscal 2014, primarily due to a portion of the Micronetics related intangible assets being fully amortized during the first quarter of fiscal 2014.

#### RESTRUCTURING AND OTHER CHARGES

In fiscal 2014, the Company announced a restructuring plan ("2014 Plan") that was implemented as part of the final phase of integration activities relating to the Company's recent acquisitions. The integration plan includes the consolidation of manufacturing facilities, centralization of administrative functions using common information systems and processes, and realignment of research and development resources. During the first quarter of fiscal 2015, the Company incurred restructuring and other charges of \$1.3 million, primarily associated with the second phase of the Chelmsford, Massachusetts headquarters consolidation and severance costs. Future restructuring expenses associated with the integration plan are expected to be approximately \$1.1 million, and the actions resulting in those charges are expected to be completed by second quarter of fiscal 2015. In the event that the Company is unable to sublease the unoccupied portion of its headquarters complex in Chelmsford, MA, it will incur nominal, periodic restructuring charges through fiscal 2017.

#### OTHER INCOME, NET

Other income, net decreased to \$0.0 million during the three months ended September 30, 2014, as compared to \$0.4 million for the same period in fiscal 2014. The decrease was driven by a \$0.3 million write off of an escrow receivable in the first quarter of fiscal 2015. Other income, net for the three months ended September 30, 2014 and 2013, also include \$0.3 million related to

the amortization of the gain on the sale leaseback of our corporate headquarters located in Chelmsford, Massachusetts. Interest income and interest expense for both periods were de minimis.

#### INCOME TAXES

We recorded income taxes of \$0.0 million during the three months ended September 30, 2014 as compared to a \$1.3 million income tax benefit for the comparable period in the prior fiscal year. Our income taxes for the three months ended September 30, 2014 differed from the federal statutory tax rate primarily due to the impact of Section 199 manufacturing deduction, stock compensation and state taxes. Our effective tax rate during the comparable period in fiscal 2014 also differed from the federal statutory rate primarily due to the impact of the federal research and development tax credits, Section 199 manufacturing deduction and stock compensation.

As of September 30, 2014, we had approximately \$10.4 million in net deferred tax assets. Each quarter, we determine the probability of realizing these assets, using significant judgments and estimates with respect to historical operating results, expectations of future earnings, tax planning strategies and other matters. If we determine in the future that there is not sufficient positive evidence to support the valuation of these assets, we may be required to adjust the valuation allowance accordingly. The Company continues to conclude that it is more likely than not that most domestic deferred tax assets would be realizable based on the current financial performance, projected future taxable income and the reversal of existing deferred tax liabilities.

The Company continues to record a full valuation allowance on certain state research and development (“R&D”) and investment tax credits, and stock basis differences as of September 30, 2014 as management continues to believe that it is not more likely than not that these deferred tax assets would be realized. Any future reversals of the valuation allowance will impact income tax expense.

#### DISCONTINUED OPERATIONS

We incurred a loss from discontinued operations of \$0.2 million in the three month ended in September 30, 2014 compared to income from discontinued operations of less than \$0.1 million for the same period in fiscal 2014.

#### SEGMENT OPERATING RESULTS

We use adjusted EBITDA as the profitability measure for our segment reporting. Adjusted EBITDA for MCE increased \$5.0 million during the three months ended September 30, 2014 to \$7.3 million as compared to \$2.3 million for the comparable period in fiscal 2014. The increase in adjusted EBITDA is driven by higher revenues of \$5.1 million primarily from defense programs, coupled with higher gross margins and lower operating expenses.

Adjusted EBITDA for MDS decreased \$0.6 million during the three months ended September 30, 2014 to \$0.5 million as compared to \$1.1 million for the comparable period in fiscal 2014. The decrease in adjusted EBITDA was primarily due to lower revenues from radar environment test and simulation sales.

See Note L to our consolidated financial statements included in this report for more information regarding our operating segments.

#### LIQUIDITY AND CAPITAL RESOURCES

Our primary source of liquidity comes from existing cash and cash generated from operations. Our near-term fixed commitments for cash expenditures consist primarily of payments under operating leases and inventory purchase commitments with our contract manufacturers. We currently do not have any material commitments for capital expenditures.

Based on our current plans and business conditions, we believe that existing cash, cash equivalents, available line of credit, cash generated from operations, and financing capabilities will be sufficient to satisfy our anticipated cash requirements for at least the next twelve months.

#### *Senior Unsecured Credit Facility*

As of September 30, 2014, there was \$86.6 million of borrowing capacity available under our credit agreement with a syndicate of commercial banks, with Key Bank National Association acting as the administrative agent. The Company can borrow up to \$200.0 million based on the Company's consolidated EBITDA for the trailing four quarters. There were no borrowings outstanding on the credit agreement; however, there were outstanding letters of credit of \$3.8 million. We were in compliance with all covenants and conditions under the credit agreement.

### Shelf Registration Statement

On August 15, 2014, we filed a shelf registration statement on Form S-3 with the SEC. The shelf registration statement, which has been declared effective by the SEC, registered up to \$500 million of debt securities, preferred stock, common stock, warrants and units. We intend to use the proceeds from a financing using the shelf registration statement for general corporate purposes, which may include the following:

- the acquisition of other companies or businesses;
- the repayment and refinancing of debt;
- capital expenditures;
- working capital; and
- other purposes as described in the prospectus supplement.

### CASH FLOWS

<u>(In thousands)</u>	As of and for the three month period ended September 30,	
	2014	2013
Net cash provided by operating activities	\$ 2,178	\$ 2,173
Net cash used in investing activities	\$ (905)	\$ (1,108)
Net cash provided by (used in) financing activities	\$ 392	\$ (61)
Net increase in cash and cash equivalents	\$ 1,589	\$ 980
Cash and cash equivalents at end of period	\$ 48,876	\$ 40,106

Our cash and cash equivalents increased by \$1.6 million from June 30, 2014 to September 30, 2014, primarily as a result of \$2.2 million in cash generated from operating activities, partially offset by \$0.9 million in purchases of property and equipment.

#### Operating Activities

During the three months ended September 30, 2014 and 2013, we generated \$2.2 million in cash from operating activities. During the three months ended September 30, 2014, we generated \$2.8 million in higher comparable net income and had a \$6.3 million decrease in cash used for payables and accrued expenses as compared to the same period in the prior year. These increases in cash generated from operations were partially offset by the timing of accounts receivable collections of \$3.6 million, \$1.4 million higher inventory purchases and \$1.3 million lower deferred revenues and customer advances. Our ability to generate cash from operations in future periods will depend in large part on profitability, the rate and timing of collections of accounts receivable, our inventory turns and our ability to manage other areas of working capital.

#### Investing Activities

During the three months ended September 30, 2014, we used \$0.9 million in investing activities compared to a use of \$1.1 million in investing activities during the same period in fiscal 2014. Both amounts represent purchases of property and equipment.

#### Financing Activities

During the three months ended September 30, 2014, we generated \$0.4 million from financing activities compared to \$0.1 million used for financing activities during the same period in fiscal 2014. The \$0.5 million change in cash from financing activities was primarily due to a \$0.3 million increase in excess tax benefits from stock-based compensation and a \$0.2 million increase in proceeds from employee stock plans during the three months ended September 30, 2014.

## COMMITMENTS AND CONTRACTUAL OBLIGATIONS

The following is a schedule of our commitments and contractual obligations outstanding at September 30, 2014:

<u>(In thousands)</u>	<u>Total</u>	<u>Less Than 1 Year</u>	<u>2-3 Years</u>	<u>4-5 Years</u>	<u>More Than 5 Years</u>
Purchase obligations	\$ 31,118	\$ 31,118	\$ —	\$ —	\$ —
Operating leases	24,483	4,881	8,338	3,701	7,563
Capital lease obligations and other	190	190	—	—	—
	<u>\$ 55,791</u>	<u>\$ 36,189</u>	<u>\$ 8,338</u>	<u>\$ 3,701</u>	<u>\$ 7,563</u>

We have a liability at September 30, 2014 of \$3.2 million for uncertain tax positions that have been taken or is expected to be taken in various income tax returns. We do not know the ultimate resolution on these uncertain tax positions and as such, do not know the ultimate timing of payments related to this liability. Accordingly, these amounts are not included in the above table.

Purchase obligations represent open non-cancelable purchase commitments for certain inventory components and services used in normal operations. The purchase commitments covered by these agreements are for less than one year and aggregated approximately \$31.1 million at September 30, 2014.

Our standard product sales and license agreements entered into in the ordinary course of business typically contain an indemnification provision pursuant to which we indemnify, hold harmless, and agree to reimburse the indemnified party for losses suffered or incurred by the indemnified party in connection with certain intellectual property infringement claims by any third party with respect to our products. Such provisions generally survive termination or expiration of the agreements. The potential amount of future payments we could be required to make under these indemnification provisions is, in some instances, unlimited.

## OFF-BALANCE SHEET ARRANGEMENTS

Other than our lease commitments incurred in the normal course of business and certain indemnification provisions, we do not have any off-balance sheet financing arrangements or liabilities, guarantee contracts, retained or contingent interests in transferred assets, or any obligation arising out of a material variable interest in an unconsolidated entity. We do not have any majority-owned subsidiaries that are not consolidated in the financial statements. Additionally, we do not have an interest in, or relationships with, any special purpose entities.

## NON-GAAP FINANCIAL MEASURES

In our periodic communications, we discuss two important measures that are not calculated according to U.S. generally accepted accounting principles (“GAAP”), adjusted EBITDA and free cash flow.

Adjusted EBITDA, the profitability measure for our segment reporting, is defined as income (loss) from continuing operations before interest income and expense, income taxes, depreciation, amortization of intangible assets, restructuring and other charges, impairment of long-lived assets, acquisition costs and other related expenses, fair value adjustments from purchase accounting and stock-based compensation costs. We use adjusted EBITDA as an important indicator of the operating performance of our business. We use adjusted EBITDA in internal forecasts and models when establishing internal operating budgets, supplementing the financial results and forecasts reported to our board of directors, determining a component of bonus compensation for executive officers and other key employees based on operating performance and evaluating short-term and long-term operating trends in our operations. We believe the adjusted EBITDA financial measure assists in providing a more complete understanding of our underlying operational measures to manage our business, to evaluate our performance compared to prior periods and the marketplace, and to establish operational goals. We believe that these non-GAAP financial adjustments are useful to investors because they allow investors to evaluate the effectiveness of the methodology and information used by management in our financial and operational decision-making.

Adjusted EBITDA is a non-GAAP financial measure and should not be considered in isolation or as a substitute for financial information provided in accordance with GAAP. This non-GAAP financial measure may not be computed in the same manner as similarly titled measures used by other companies. We expect to continue to incur expenses similar to the adjusted EBITDA financial adjustments described above, and investors should not infer from our presentation of this non-GAAP financial measure that these costs are unusual, infrequent or non-recurring.

The following table reconciles our income (loss) from continuing operations, the most directly comparable GAAP financial measure, to our adjusted EBITDA:

<u>(In thousands)</u>	Three Months Ended September 30,	
	2014	2013
Income (loss) from continuing operations	\$ 717	\$ (2,304)
Interest expense, net	5	14
Tax benefit	—	(1,319)
Depreciation	1,700	1,974
Amortization of intangible assets	1,762	1,985
Restructuring and other charges	1,268	(15)
Stock-based compensation cost	2,551	2,988
Adjusted EBITDA	<u>\$ 8,003</u>	<u>\$ 3,323</u>

Free cash flow, a non-GAAP measure for reporting cash flow, is defined as cash provided by operating activities less capital expenditures for property and equipment. We believe free cash flow provides investors with an important perspective on cash available for investments and acquisitions after making capital investments required to support ongoing business operations and long-term value creation. We believe that trends in our free cash flow are valuable indicators of our operating performance and liquidity.

Free cash flow is a non-GAAP financial measure and should not be considered in isolation or as a substitute for financial information provided in accordance with GAAP. This non-GAAP financial measure may not be computed in the same manner as similarly titled measures used by other companies. We expect to continue to incur expenditures similar to the free cash flow adjustment described above, and investors should not infer from our presentation of this non-GAAP financial measure that these expenditures reflect all of our obligations which require cash.

The following table reconciles cash provided by operating activities, the most directly comparable GAAP financial measure, to free cash flow:

<u>(In thousands)</u>	Three Months Ended September 30,	
	2014	2013
Cash provided by operating activities	\$ 2,178	\$ 2,173
Capital expenditures for property and equipment	(905)	(1,108)
Free cash flow	<u>\$ 1,273</u>	<u>\$ 1,065</u>

#### RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In August 2014, the FASB issued ASU No. 2014-15, *Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern*, an amendment of the FASB Accounting Standards Codification. The ASU has added additional disclosure requirements to the codification. It requires management to assess, at each interim and annual reporting period, whether substantial doubt exists about the company's ability to continue as a going concern. Substantial doubt exists if it is probable (the "probable" threshold under US GAAP has generally been interpreted to be between 75 and 80 percent) that the company will be unable to meet its obligations as they become due within one year after the date the financial statements are issued or available to be issued (assessment date). The ASU is effective for annual reporting periods beginning after December 15, 2016, and interim periods thereafter, with early adoption permitted. We do not expect a going concern problem in the foreseeable future, and therefore this guidance is not expected to have a material impact to our consolidated financial statements.

#### RECENTLY ADOPTED ACCOUNTING PRONOUNCEMENTS

Effective July 1, 2014, we adopted FASB ASU No. 2013-11, *Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists*, an amendment of the FASB Accounting Standards Codification. The ASU requires an unrecognized tax benefit to be presented as a decrease in a deferred tax asset when net operating loss carryforwards, similar tax losses, or tax credit carryforwards exist and certain criteria are met. Such adoption did not have a material impact to our consolidated financial statements.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

There were no material changes in our exposure to market risk from June 30, 2014 to September 30, 2014.

**ITEM 4. CONTROLS AND PROCEDURES**

*(a) Evaluation of Disclosure Controls and Procedures*

We conducted an evaluation under the supervision and with the participation of our management, including the Chief Executive Officer and Chief Financial Officer (our principal executive officer and principal financial officer, respectively), regarding the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 as amended (the “Exchange Act”)) as of the end of the period covered by this report. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective as of September 30, 2014. We continue to review our disclosure controls and procedures and may from time to time make changes aimed at enhancing their effectiveness and to ensure that our systems evolve with our Company’s business. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

*(b) Changes in Internal Control Over Financial Reporting*

There was no change in our internal control over financial reporting (as defined in Rules 13c-15(f) and 15d-15(f) under the Exchange Act) that occurred during the quarter ended September 30, 2014 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.



## PART II. OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

We are subject to litigation, claims, investigations and audits arising from time to time in the ordinary course of our business. Although legal proceedings are inherently unpredictable, we believe that we have valid defenses with respect to those matters currently pending against us and intend to defend our self vigorously. The outcome of these matters, individually and in the aggregate, is not expected to have a material impact on our cash flows, results of operations, or financial position.

### ITEM 1A. RISK FACTORS

You should carefully review and consider the information regarding certain factors that could materially affect our business, financial condition or future results set forth under Item 1A (Risk Factors) in our Annual Report on Form 10-K for the fiscal year ended June 30, 2014. There have been no material changes from the factors disclosed in our 2014 Annual Report on Form 10-K filed on August 14, 2014, although we may disclose changes to such factors or disclose additional factors from time to time in our future filings with the Securities and Exchange Commission.

### ITEM 6. EXHIBITS

The following Exhibits are filed or furnished, as applicable, herewith:

- |       |   |
|-------|---|
| 10.1  | Amended and Restated Performance-Based Restricted Stock Award Agreement under the 2005 Plan   |
| 10.2  | Separation Agreement, dated as of September 3, 2014 by and between the Company and Kevin M. Bisson  |
| 31.1  | Certification of the Company's Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002  |
| 31.2  | Certification of the Company's Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002  |
| 32.1+ | Certification of the Company's Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002  |
| 101   | The following materials from the Company's Quarterly Report on the Form 10-Q for the quarter ended September 30, 2014 formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Balance Sheets; (ii) the Consolidated Statements of Operations; (iii) the Consolidated Statements of Cash Flows; and (iv) notes to the Consolidated Financial Statements |
| +     | Furnished herewith. This certificate shall not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, or otherwise subject to the liability of that section, nor shall it be incorporated by reference into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934.   |

**MERCURY SYSTEMS, INC.**

**Signatures**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, in Chelmsford, Massachusetts, on November 6, 2014.

MERCURY SYSTEMS, INC.

By:

/s/ GERALD M. HAINES II

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**Gerald M. Haines II**

**Executive Vice President,**

**Chief Financial Officer, and Treasurer**

AMENDED AND RESTATED PERFORMANCE RESTRICTED STOCK AWARD AGREEMENT

UNDER THE MERCURY SYSTEMS, INC.  
2005 STOCK INCENTIVE PLAN

Name of Grantee:  
No. of Shares:  
Grant Date:  
Final Acceptance Date:

Pursuant to the Mercury Systems, Inc. 2005 Stock Incentive Plan (the "Plan") as amended through the date hereof, Mercury Systems, Inc. (the "Company") hereby grants a Restricted Stock Award (an "Award") to the Grantee named above. Upon acceptance of this Award, the Grantee shall receive the number of shares of Common Stock, par value \$0.01 per share (the "Stock"), of the Company specified above, subject to the restrictions and conditions set forth herein and in the Plan.

1. Acceptance of Award. The Grantee shall have no rights with respect to this Award unless he or she shall have accepted this Award prior to the close of business on the Final Acceptance Date specified above by (i) signing and delivering to the Company a copy of this Award Agreement and (ii) delivering to the Company a stock power endorsed in blank. Upon acceptance of this Award by the Grantee, the shares of Restricted Stock so accepted shall be issued and held by the Company's transfer agent in book entry form, and the Grantee's name shall be entered as the shareholder of record on the books of the Company. Thereupon, the Grantee shall have all the rights of a shareholder with respect to such shares, including voting and dividend rights, subject, however, to the restrictions and conditions specified in Paragraph 2 below.

2. Restrictions and Conditions.

(a) Any book entries for the shares of Restricted Stock granted herein shall bear an appropriate legend, as determined by the Administrator in its sole discretion, to the effect that such shares are subject to restrictions as set forth herein and in the Plan.

(b) Shares of Restricted Stock granted herein may not be sold, assigned, transferred, pledged or otherwise encumbered or disposed of by the Grantee prior to vesting.

(c) If Grantee's employment with the Company and its Subsidiaries is voluntarily or involuntarily terminated for any reason (including death) prior to vesting of shares of Restricted Stock granted herein, all non-vested shares shall be automatically forfeited to the Company.

3. Vesting of Restricted Stock.

(a) The restrictions and conditions in Paragraph 2 of this Agreement shall lapse on the Vesting Date or Dates specified in the following schedule. If a series of Vesting Dates is specified, then the restrictions and conditions in Paragraph 2 shall lapse only with respect to the number of shares of Restricted Stock specified as vested on such date.

[insert performance vesting schedule]

(b) The restrictions and conditions in Paragraph 2 of this Agreement shall lapse upon the occurrence of a Change of Control of the Company.

4. Dividends. Dividends on Shares of Restricted Stock shall be paid currently to the Grantee.

5. Incorporation of Plan. Notwithstanding anything herein to the contrary, this Agreement shall be subject to and governed by all the terms and conditions of the Plan, including the powers of the Administrator set forth in Section 3 of the Plan. Capitalized terms in this Agreement shall have the meaning specified in the Plan, unless a different meaning is specified herein.

6. Transferability. This Agreement is personal to the Grantee, is non-assignable and is not transferable in any manner, by operation of law or otherwise, other than by will or the laws of descent and distribution.

7. Tax Withholding. The Grantee shall, not later than the date as of which the receipt of this Award becomes a taxable event for Federal income tax purposes, pay to the Company or make arrangements satisfactory to the Administrator for payment of any Federal, state, and local taxes required by law to be withheld on account of such taxable event. The Grantee may elect to have the required minimum tax withholding obligation satisfied, in whole or in part, by (i) authorizing the Company to withhold from shares of Stock to be issued, or (ii) transferring to the Company, a number of shares of Stock with an aggregate Fair Market Value that would satisfy the withholding amount due.

8. Miscellaneous.

(a) Notice hereunder shall be given to the Company at its principal place of business, and shall be given to the Grantee at the address set forth below, or in either case at such other address as one party may subsequently furnish to the other party in writing.

(b) This Agreement does not confer upon the Grantee any rights with respect to continuation of employment by the Company or any Subsidiary.

MERCURY SYSTEMS, INC.

By:

Title:

The foregoing Agreement is hereby accepted and the terms and conditions thereof hereby agreed to by the undersigned.

Dated: \_\_ \_\_

Grantee's Signature

Grantee's name and address:

**SEPARATION AGREEMENT**

September 3, 2014

Kevin Bisson  
25 Baldpate Road  
Boxford, MA 01921

Dear Kevin,

Mercury Systems, Inc. (the "Company") will terminate your employment effective September 5, 2014, (the "Separation Date"). This letter outlines the special severance package that the Company will provide you in connection with your separation from employment.

**Special Severance Package.**

In consideration of your acceptance of all of the terms and conditions of this Separation Agreement (the "Agreement"), and subject to your performance hereunder, the Company will provide you with the following Special Severance Package, provided you execute and deliver this Agreement to the Company (Attention: Joe Freitas) within twenty-one (21) days of your receipt of this Agreement (but only after the Separation Date) and the applicable revocation period has passed:

a. The Company will pay your regular base salary for a period of 52 week(s), less legally-required and voluntarily-authorized deductions (the "Salary Continuation"). This Salary Continuation will begin following the Effective Date of this Agreement and after receipt of your signed Separation Agreement and expiration of the 7 day revocation period, and provided you do not choose to revoke this agreement during such revocation period. Notwithstanding the preceding sentence, the Company will voluntarily continue to pay you your regular salary for the first two (2) weeks after the Separation Date even if you have not yet satisfied conditions in the preceding paragraph, subject to the conditions that (1) such payments shall be included and accounted for as part of the Salary Continuation, and (2) the fact that the Company made such payments shall in no way obligate the Company to continue to make any such payments after such two-(2)-week period. You will be paid in equal installments on the Company's regularly scheduled Paydays;

b. Your current medical, dental, and vision insurance will continue with the Company paying the same portion of your premium as it pays with respect to active employees for the period of Salary Continuation, or until you obtain benefits through another employer, whichever occurs first. Following that, you will be eligible to continue medical, dental, and vision coverage under COBRA; and

c. The Company will provide you with up to \$45,000 of executive outplacement services, provided you begin to use these services no later than six months from your termination date;

d. The Company will waive any obligation that you reimburse the Company for tuition payments previously reimbursed to you, any signing bonus or any relocation or immigration assistance paid or provided to you by the Company that would otherwise be required in connection with the termination of your employment; and

e. The Company agrees that when asked for a company reference for your future employment the following directory information will be given as the response:  
"Mr. Bisson was our Sr. Vice President, Chief Financial Officer & Treasurer from January 11, 2012 to September 5, 2014. As a policy we do not give company references." You agree that you will direct all reference requests to the Company's Vice President of Human Resources.

**Employee Acknowledgements.**

Your participation in all other employee benefit plans of the Company terminated on the Separation Date. By signing this Agreement, you acknowledge and agree that you have been paid all wages due and owing to you from the Company, You affirm that you have no known workplace injuries or occupational diseases and have not been denied any leave required under the Family and Medical Leave Act or any state law corollary.

**General Release.**

In exchange for the Special Severance Package offered to you under this Agreement, to which you acknowledge and agree that you are not otherwise entitled, you hereby release the Company and all of its predecessor, successor, parent, subsidiary, affiliated and related companies and all of their present, former and future directors, officers, trustees, members, attorneys, employees, shareholders, agents, successors, assigns and representatives, individually and in their official capacities (collectively referred to as the "Releasees") from any and all claims known or unknown, suspected or unsuspected, arising or which may have existed at any time to this date, whether in law or equity, including, but not limited to, any claims arising from any alleged violation by Releasees of any federal, state or local statutes, ordinance or common laws, specifically including, but not limited to, the Age Discrimination in Employment Act of 1967, the Older Workers Benefit Protection Act, the Worker Adjustment and Retraining Notification Act, Title VII of the Civil Rights Act of 1964, the Civil Rights Act of 1991, the Employee Retirement Income Security Act of 1974, the Americans with Disabilities Act of 1990, the Occupational Safety and Health Act, the Family and Medical Leave Act, the Massachusetts Fair Employment Practices Act, the Massachusetts Equal Pay Law, the Massachusetts Age Discrimination Law, the Massachusetts Equal Rights for Elderly and Disabled Law, the Massachusetts Equal Rights Act, the Massachusetts Civil Rights Act, the Massachusetts Privacy Statute, the Massachusetts Consumer Protection Act, the Massachusetts Constitution, Massachusetts common law and any and all other federal, state, county or local ordinances, statutes or regulations, all as may be amended, and any other claim relating to or arising out of your employment with or separation from the Company.

**Exclusions from General Release; Covenant Not To Sue.**

You also covenant not to sue Releasees on any claim covered by the foregoing release, provided that this covenant will not apply to claims under the Age Discrimination in Employment Act. Thus, any legal action challenging this Agreement that directly pertains to the Age Discrimination in Employment Act is not prohibited by this covenant not to sue, and such legal action would not constitute a breach of this Agreement. You agree that neither you nor any of your heirs, representatives, or assigns has asserted in any forum any of the claims described in the foregoing paragraph. You further agree that neither you nor any of your heirs, representatives, or assigns will assert in any forum any of the claims described in the foregoing paragraph, except that you may challenge the validity of this release under the Age Discrimination in Employment Act and you may file a charge with an administrative agency or as otherwise permitted by law. Notwithstanding the generality of this paragraph, the above release and waiver of claims applies to the extent permitted by law and, in the event any charge or claim is permitted by law, you expressly waive your right to recover any relief, damages, and/or monetary benefit as a result of any such charge or claim. This Agreement is not intended to, and does not, govern any claims that cannot be released by private agreement.

To the extent permitted by law, you agree that you have not and shall not in any manner or by any means, directly or indirectly, instigate, initiate, promote, counsel, encourage, testify, provide evidence or information, aid or assist in: (a) any investigations, actions, disputes, differences, grievances, suits, causes of action, complaints or claims against or relating to Releasees; or (b) any activity detrimental to the interests or goodwill of Releasees, unless under a subpoena or court order to do so. Nothing in this Agreement shall prohibit or restrict you from (a) providing information to, or otherwise assisting in, an investigation by the United States Congress, the Securities and Exchange Commission ("SEC"), the Equal Employment Opportunity Commission ("EEOC"), the National Labor Relations Board ("NLRB"), the Massachusetts Commission Against Discrimination, or any other federal regulatory or law enforcement agency or self-regulatory organization ("SRO") and/or (b) testifying, participating, or otherwise assisting in a proceeding relating to an alleged violation of any federal law relating to fraud or any rule or regulation of the SEC, EEOC, NLRB, MCAD or any SRO.

**Non-Disclosure/Non-Disparagement.**

You agree that you will not disclose, directly or indirectly, the existence of this Agreement or any terms or provisions of this Agreement, except: (a) to members of your immediate family, on the condition that they be advised that they cannot further disclose the same to others; (b) as may be necessary to obtain professional legal and/or tax advice; and (c) as required by applicable law. For purposes of this paragraph, "immediate family" includes spouse, parents and children. By executing this Agreement, your signature affirms that you have not previously breached this paragraph.

You agree that you will not disparage Releasees by stating, suggesting, implying, doing

or saying anything that could in any way be harmful to the business interests or good will of Releasees.

### **Protection of Confidential Information.**

You further agree that you will never, directly or indirectly, use or disclose any Confidential Information of Releasees. For purposes of this Agreement, "Confidential Information" is defined as any and all information not generally known to others with whom Releasees do business, or plan to compete or do business (including, without limitation, information related to Releasees' services, customers, customer lists, markets, developments, inventions, processes, formulas, technology, marketing, finances and all other business information), and also includes comparable information that Releasees receive or have received belonging to others who do business with Releasees. This obligation specifically includes, but is not limited to, information protected from disclosure by the Health Insurance Portability and Accountability Act ("HIPAA"), the Americans with Disabilities Act ("ADA") and all other federal and state laws governing the confidentiality of employee information. Confidential Information includes all information that Releasees receive or have received from others with any understanding, express or implied, that it will not be disclosed. Confidential Information also includes information regarding the policies and practices of Releasees, and any actual, threatened or perceived claims, lawsuits, charges, and internal or external investigations relating to Releasees. You acknowledge and recognize that any disclosure of Confidential Information by you may give rise to irreparable injury to Releasees, which may not be adequately compensated by monetary damages, and that Releasees shall be entitled, in addition to any other damages, to obtain without posting a bond, an injunction restraining you from disclosing, in whole or in part, the Confidential Information (or from rendering services to any person or entity to whom such Confidential Information, in whole or in part, may be or has been disclosed).

### **Return of Company Property.**

You agree to return to the Company all the Company property, including without limitation, mailing lists, reports, computer and paper files, memoranda, records, computer hardware, software, data, cellular telephones, credit cards, door and file keys, computer access codes or disks and instructional manuals, and other physical or personal property which you received or prepared or helped prepare in connection with your employment with the Company, and that you will not retain any copies, duplicates, reproductions or excerpts thereof.

### **Assignment of Intellectual Property.**

You hereby assign to the Company any right, title and interest to all Intellectual Property. You agree to execute any and all applications for domestic or foreign patents, copyrights, and other proprietary rights and to do such other acts (including, among others, the execution and delivery of instruments of further assurance or confirmation) requested by the Company to assign the Intellectual Property to the Company and to permit the Company to enforce any patents, copyrights and other proprietary rights in the Intellectual Property. You will not charge the Company for time spent in complying with these obligations. For purposes of this Agreement, "Intellectual Property" means inventions, copyrightable works, discoveries, developments, clinical and other research materials, methods, processes, compositions, works, concepts and ideas (whether or not patentable or copyrightable or constituting trade secrets) conceived, made, created, developed or reduced to practice by you (whether alone or with others) during your employment that relate in any way to the business, products or services of the Company or to any prospective activity of the Company, or which were assisted in any way by Company resources or facilities. Intellectual Property includes, without limitation, all Confidential Information. Furthermore, you acknowledge and agree that, without obtaining prior written authorization from the Company's Chief Legal Officer, you are prohibited from (a) publishing any information or materials related to or arising out of your employment at the Company, and (b) mentioning the Company in any published work.

### **Non-Competition Covenant.**

By signing this Agreement, you agree that for a period of [twelve (12)] months after the Separation Date, you will not, directly or indirectly, develop, design, produce, market or sell (or assist any other person in developing, designing, producing, marketing or selling) products or perform services competitive with those developed (or under development), designed, produced, marketed, sold or performed, including those products or services known to be planned or analyzed for future production, sale or performance, by the Company. You agree that the business of the Company is nationwide in scope and that the type of products and services provided by the Company can be provided from any location in the United States for the benefit of customers located anywhere in the United States. Thus, you agree that the business non-solicitation and non-competition obligations contained in this Agreement shall restrict your competitive activities throughout the United States and with respect to the Company's entire customer base.

### **Non-Solicitation Covenants.**

By signing this Agreement, you further agree that for a period of twelve (12) months after the Separation Date, you will not, directly or indirectly:

(a) Recruit, solicit or hire any person who is at that time or was within the previous twelve (12) months providing services to the Company as an employee, a contractor, a subcontractor or an agent or employee of any such contractor or subcontractor, or induce or attempt to induce any such person to terminate his or her employment with, or otherwise cease his or her relationship with, the Company, or cooperate with or provide information to any person or entity that may recruit, solicit or hire any such person; or

(b) Solicit, divert or take away, or attempt to solicit, divert or take away, the business or patronage of any of the customers, clients or accounts, or prospective customers, clients or accounts, of the Company,

### **Enforcement of Covenants.**

You agree that if you violate any of the foregoing covenants, then in addition to all other remedies that may be available and damages that may be awarded to the Company, you shall continue to be bound by the restrictions set forth in such covenant until a period of twelve (12) months has expired without any violation of such provision. You further acknowledge that the scope of prohibited activities and time duration of these restrictions are reasonable in nature and are no broader than are necessary to maintain the goodwill of the Company and the confidentiality of its Confidential Information and to protect the other legitimate business interests of the Company. You further acknowledge that assertion of a breach of this Agreement by the Company shall not serve as a defense to claims arising from the Company's enforcement of this Agreement.

### **No Admission.**

You acknowledge and agree that the existence and execution of this Agreement shall not be considered as an admission by Releasees of any liability, error, violation or omission. You agree not to represent or imply to anyone that Releasees took any action with respect to you that was unlawful or wrongful, or violated any federal or state law, order, policy, rule, or regulation.

### **Cooperation.**

You agree that, following the separation of your employment with the Company, you will cooperate fully with the Company, upon request, in relation to the defense, prosecution or other involvement by the Company, in any continuing or future claims, lawsuits, charges, audits and internal or external investigations that arise out of events or business matters that occurred during your employment with the Company. This continuing duty of cooperation shall include you being available to the Company, upon reasonable notice, for depositions, interviews and appearances as a witness, and furnishing information to the Company and its legal counsel upon request. The Company agrees to reimburse you for reasonably documented travel, food, and lodging expenses in connection with the aforementioned cooperation. If you are employed at a new employer, you shall not be required, in connection with the aforementioned cooperation, to be absent from your employment in a manner that causes you to lose wages or to use up paid vacation time granted to you by your new employer unless you are fairly compensated for such lost wages or lost paid-vacation time.

### **Entire Agreement.**

This Agreement constitutes the entire agreement between you and Releasees and supersedes all prior and contemporaneous agreements, communications and understandings, written or oral, with respect to all matters including, but not limited to, your employment and its separation, provided that this Agreement shall not terminate or supersede any ongoing obligations you may have pursuant to any and all agreements between you and the Company that exist on the date of this Agreement.

### **Understanding/Governing Law.**



In signing this Agreement, you give the Company assurance that you have read and understand all provisions of this Agreement and that you have signed this Agreement freely and voluntarily. You acknowledge and understand that this Agreement will be governed by and interpreted in accordance with the laws of The Commonwealth of Massachusetts. If any portion of this Agreement shall to any extent be declared unenforceable or illegal by a court of competent jurisdiction, the remainder of this Agreement shall not be affected thereby, and each portion and provision of this Agreement shall be valid and enforceable to the fullest extent permitted by law.

### **Remedies Upon Breach.**

You agree and understand that if you breach any term of this Agreement, in addition to all other remedies available to Releasees in law and in equity, the Company shall be entitled to: (a) the return of any and all consideration paid to you pursuant to this Agreement (less \$500 or 10% of such consideration, whichever is less), to the extent permitted by law; (b) discontinue its obligations under this Agreement; (c) recover any and all expenses (including costs and attorneys' fees) incurred in recovering any and all consideration paid to you pursuant to this Agreement; and (d) obtain a court order enforcing the breached provision(s) of this Agreement. You further understand that you could be held liable in monetary damages to Releasees for any action constituting a breach under this Agreement. This paragraph does not limit the right of Releasees to sue for breach of this Agreement and obtain injunctive relief in connection therewith, nor does it limit your right to sue for breach of this Agreement and obtain injunctive relief in connection therewith. You acknowledge and agree that the return of any consideration paid to you pursuant to this Agreement shall not affect the validity of this Agreement. You shall have no automatic repayment obligations if you were to challenge the Age Discrimination in Employment Act waiver only.

### **Consideration/Revocation.**

The Company wants to be certain that this Agreement, and the Special Severance Package provided hereunder, will resolve any concerns you may have and therefore encourages you to carefully consider the terms of this Agreement and to seek the advice of an attorney before signing it.

You acknowledge that you have had a period of at least twenty-one (21) days to consider the terms of this Agreement. However, you may sign this Agreement and return it to me at any time after the Separation Date and within this twenty-one (21) day period. You may revoke this Agreement during the seven (7) days immediately following your execution of this Agreement by submitting a revocation, in writing, to me. If you do not revoke this Agreement prior to the expiration of this seven (7) day period, this Agreement shall take effect at that time as a legally binding agreement between you and the Company on the basis set forth herein (the "Effective Date").

If you accept the terms of this Agreement, please sign below and return this Agreement to me on or before the first business day following the twenty-first (21) day after your receipt of this Agreement (but only after the Separation Date).

YOU ARE HEREBY ADVISED THAT YOU HAVE TWENTY-ONE (21) CALENDAR DAYS TO REVIEW THIS AGREEMENT AND GENERAL RELEASE AND ANY AND ALL INFORMATION PROVIDED, AND ARE HEREBY ADVISED TO CONSULT WITH AN ATTORNEY PRIOR TO EXECUTION OF THIS AGREEMENT AND GENERAL RELEASE.

HAVING ELECTED TO EXECUTE THIS AGREEMENT AND GENERAL RELEASE, TO FULFILL THE PROMISES AND TO RECEIVE THE SUMS AND BENEFITS ABOVE, YOU FREELY AND KNOWINGLY, AND AFTER DUE CONSIDERATION, ENTER INTO THIS AGREEMENT AND GENERAL RELEASE INTENDING TO WAIVE, SETTLE AND RELEASE ALL CLAIMS YOU HAVE OR MIGHT HAVE AGAINST MERCURY SYSTEMS, INC. AND RELEASEES.

Sincerely,

/s/ Joe Freitas

Joe Freitas  
VP, Human Resources

This is a legal document. You have been advised to consult with an attorney prior to executing this Agreement.

By signing this Separation Agreement, you acknowledge and affirm that you are competent, that you were provided at least twenty-one (21) days to review and consider this Separation Agreement with an attorney of your choice, that you have read and understand and accept this document as fully and finally waiving and releasing any and all claims and rights which you may have against Releasees (as defined above), including any and all claims and rights under the Age Discrimination in Employment Act, that you have received and understood all information required by the Age Discrimination in Employment Act, that no promises or inducements have been made to you except as set forth in this Separation Agreement, and that you have signed this Separation Agreement freely, knowingly and voluntarily, intending to be legally bound by its terms

Intending to be legally bound, I have signed this Agreement as of the date set forth below.

Signature: /s/ Kevin Bisson

Name: Kevin Bisson  
(please print)

Date: 9/23/14

## CERTIFICATION

I, Mark Aslett, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Mercury Systems, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 6, 2014

/s/ MARK ASLETT

Mark Aslett

**PRESIDENT AND CHIEF EXECUTIVE OFFICER  
[PRINCIPAL EXECUTIVE OFFICER]**

## CERTIFICATION

I, Gerald M. Haines II, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Mercury Systems, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 6, 2014

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/s/ GERALD M. HAINES II  
Gerald M. Haines II  
EXECUTIVE VICE PRESIDENT,  
CHIEF FINANCIAL OFFICER, AND TREASURER  
[PRINCIPAL FINANCIAL OFFICER]

Mercury Systems, Inc.

Certification Pursuant To  
18 U.S.C. Section 1350,  
As Adopted Pursuant To  
Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Quarterly Report of Mercury Systems, Inc. (the "Company") on Form 10-Q for the period ended September 30, 2014 as filed with the Securities and Exchange Commission (the "Report"), we, Mark Aslett, President and Chief Executive Officer of the Company, and Gerald M. Haines II, Executive Vice President, Chief Financial Officer, and Treasurer of the Company, certify, pursuant to Section 1350 of Chapter 63 of Title 18, United States Code, that to our knowledge the Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934, as amended, and the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 6, 2014

/s/ MARK ASLETT

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Mark Aslett

**PRESIDENT AND CHIEF EXECUTIVE OFFICER**

/s/ GERALD M. HAINES II

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Gerald M. Haines II

**EXECUTIVE VICE PRESIDENT,  
CHIEF FINANCIAL OFFICER, AND TREASURER**

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

