



DEPARTMENT OF DEFENSE  
OFFICE OF GENERAL COUNSEL  
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June 6, 2013

Michael Moiseyev  
Assistant Director  
Bureau of Competition  
Federal Trade Commission  
600 Pennsylvania Avenue, NW  
Washington, DC 20580

Dear Mr. Moiseyev:

This is in response to your letter of June 6, 2013, in which you presented the Federal Trade Commission's competitive analysis of the proposed acquisition of United Technology's Pratt & Whitney Rocketdyne (PWR) by Gencorp's Aerojet-General Corporation (AJ). Of particular Commission concern is the competitive impact of the combination of the only two current domestic providers of Liquid Divert and Attitude Control Systems (LDACS), resulting in a monopoly for LDACS. While the Department of Defense recognizes that allowing the transaction to go forward without remedying its anticompetitive effects in the LDACS market would not be the normal course for the Commission, the Department nevertheless requests that the transaction be allowed to proceed for both national security and industrial base reasons.

As a threshold matter, the Department believes that there may not be significant competitive opportunities for LDACS in the near- or mid-term; the lack of future competitive opportunities would mitigate the anticompetitive impact of a merger to monopoly. We understand, however, that the Commission staff has concluded that future LDACS competition, at least for development, is sufficiently likely so as to raise competitive concerns. Assuming the Commission view that future LDACS competitions are likely, the Department understands that the next step in the ordinary course of a transaction review would be to seek a structural remedy to the LDACS merger-to-monopoly situation. Such a remedy, however, is impossible due to highly unusual national security circumstances.

The LDACS are critical components of the Exo-atmospheric Kill Vehicles, which are in turn critical elements of the nation's missile defense system. The Missile Defense Agency (MDA) has identified significant national security concerns with any disruption in the production lines of either of the LDACS suppliers. For both technical and geopolitical reasons, neither of which is appropriate to discuss in an unclassified environment, there cannot be any perturbations in the production lines or delivery schedules of either the AJ or PWR LDACS product. A near-term divestiture of either LDACS business unit would invariably create disruption for that product line; at a minimum, employees would be distracted, affecting both productivity and reliability, and worst case, any disturbance of production capabilities could cause unidentified faults or failures in fielded systems designed to protect the U.S. homeland against



intercontinental ballistic missiles or U.S. and allied forces abroad against short-range and medium-range ballistic missiles.

Hence, a near-term divestiture of either LDACS business unit is not possible as a matter of national security; the risk to the nation's security is too great to justify a divestiture to preserve competition. Consequently, a structural remedy to the anticompetitive impact of this merger is impossible. Standing alone, this situation could result in a conclusion that the transaction should be blocked. The Department, however, urges the Commission to consider the overall national security and industrial base benefits of this transaction as counterbalancing the loss of competition in a small niche market.

The transaction as a whole offers non-pecuniary benefits to the Department that could not be achieved without the merger going forward. Specifically, the merger of these two liquid rocket engine (LRE) manufacturers in a market projected to contract with no foreseeable competitive program and an excess of capacity will preserve the LRE industrial base, which is critical for continued U.S. access to space, a national security objective. Combining these two companies will enable consolidation and rationalization of LRE facilities and preservation of intellectual capital by combining the highly specialized scientists and engineers on collaborative projects that would, absent the merger, be restricted to one company or the other. Notwithstanding the dearth of competitive LRE opportunities in the future, the Department has a continuing national security need for LREs. It is, therefore, critical to national security that robust LRE capability be maintained in the combined company.

The Department understands that economic efficiencies claimed by the parties may well be overstated. As the primary customer for LREs, however, the Department bears most of the overhead costs of these companies. In an era of declining budgets, the financial constraints on the Department's space launch capability are substantial. Thus, any efficiency that can be derived from this transaction, whether economic or otherwise and no matter how small, is important to the Department.

Of greater importance to the Department than the efficiencies, however, is the sustainment of a robust LRE industrial base, and the sustainment of the "best and the brightest" intellectual talent and capabilities of each company. Both companies have uniquely trained and experienced liquid propulsion scientists and engineers, as well as the specialized infrastructure required to develop, test, and produce medium and large liquid rocket engines. The current LRE market has already contracted to the point that both companies are maintaining the minimum intellectual capital required to sustain their current LRE efforts. While the Department envisions little, if any, increase in its future LRE requirements, it does consider it critical that the combined company maintain the knowledge derived from prior and ongoing research, development, and production efforts. By consolidating the companies, technical challenges and opportunities can be made available to a wider base of scientists and engineers, providing a two-fold benefit: obtaining a "best of breed" solution to the technical issues and, probably more importantly, providing intellectual challenges to the scientists and engineers to keep them actively engaged in the LRE business, particularly those who have developed expertise in the government-funded technology of hydrocarbon LREs.

The Department supports this transaction, viewing it as a means to preserve the LRE industrial base by retaining the people and the research the Air Force has funded to develop expertise in various high technology areas associated with LRE development, while potentially reducing the overhead costs of contractors, in turn reducing costs to the government, in an increasingly fiscally constrained environment. The combined company will be better prepared to address the contraction in the liquid rocket engine market; it will have the flexibility to optimize its capacity most cost-effectively, while preserving vital liquid rocket engine capabilities. As a result of its previous internal reorganization, AJ has demonstrated an ability to rationalize efficiently and to manage a low-demand LRE industrial sector, while effectively sustaining essential design and engineering capabilities necessary to develop future systems. The Department anticipates that AJ will be able to rationalize the combined company's LRE design and engineering capabilities, while preserving critical hydrocarbon engine skills.

In summary, the Department wishes to see the transaction go forward to sustain the industrial base for LREs, a critical capability for national security, while MDA, for purely national security reasons, does not want any disruption whatsoever in the LDACS market, the one area in which the transaction creates competitive problems. In view of the overall benefit to the Department from the potential rationalization that should occur in the LRE industrial base, and the less significant harm to the Department's interests from any monopolistic behavior that the merged company might attempt in the LDACS market, the Department requests that the Commission allow AJ to acquire PWR despite the anticompetitive result in the LDACS market.

I would welcome the opportunity to meet with you to discuss this request. As has been the case for many years, I appreciate the cooperative and collaborative relationship that our two organizations have enjoyed over the course of many, many transaction reviews. Thank you for your consideration of this matter.

Sincerely,



Susan P. Raps  
Deputy General Counsel  
(Acquisition & Logistics)