June 29, 2018

Chairman Joseph J. Simons
Commissioner Maureen K. Ohlhausen
Commissioner Noah Joshua Phillips
Commissioner Rohit Chopra
Commissioner Rebecca Kelly Slaughter
Federal Trade Commission
Office of the Secretary
600 Pennsylvania Avenue NW
Suite CC-5610 (Annex D)
Washington, D.C. 20024

RE: In the Matter of Northrop Grumman Corporation and Orbital ATK, Inc., File No. 181 0005

Dear Chairman Simons and Commissioners,

In its recent settlement resolving charges that Northrop Grumman's ("Northrop's") $7.8 billion acquisition of aerospace and defense contractor Orbital ATK ("Orbital") likely would be anticompetitive, the Commission opened its consent order (the "Order") to public comment. Aerojet Rocketdyne writes this comment to express its concern that the Order will end competition in the solid rocket motor ("SRM") market.

The Order focused on preventing the combined Orbital and Northrop from "favor[ing] its now vertically integrated missile system business" and "offer[ing] its SRMs at disadvantageous terms, thereby raising rivals' costs or otherwise undermining their ability to compete on future missile system bids . . . by prohibiting Northrop from discriminating against competing missile prime customers in supplying SRMs."[1] The non-discrimination provisions of the Order are broad "and apply to any potential discriminatory conduct affecting price, schedule, quality, data, personnel, investment, technology, innovation, design, or risk."[2] In essence, the Order sought to ensure that prime contractors other than Northrop have access to Orbital's SRMs at fair, reasonable and nondiscriminatory prices.

In accomplishing its intended purpose, the Order in effect encourages all prime contractors to simply choose SRMs from Northrop's new Orbital subsidiary (which Northrop has named Northrop Grumman Innovation Systems "NGIS") and not conduct a competitive bidding process. Northrop acquired Orbital to vertically integrate its SRM business to, at least in-part, save on the costs related to any SRM portion of a missile program that Northrop will bid on as a prime contractor. Other prime contractors, who will all be bidding on programs that include SRMs as one input, will view the non-discriminatory requirements of the Order as requiring NGIS to provide SRMs at the vertically-integrated prices that

[1] Northrop Grumman Corporation and Orbital ATK, Inc.; Analysis To Aid Public Comment, 83 Fed. Reg. 27777 (June 14, 2018).
[2] *Id.* at 27778.

Northrop will receive. With a low-cost offer mandated by the Order that is on par with Northrop's SRM cost in its bid, the prime contractors have no incentive to consider SRM providers other than NGIS when creating their bids. The Order in effect requires Northrop's vertically-integrated SRM provider (NGIS) to provide its low-cost vertically integrated priced SRMs to all other prime contractors. Knowing that NGIS will provide a strong SRM package to its parent Northrop, other prime contractors will demand that NGIS provide the same terms for SRMs as it gives to itself. Consequently, the Federal Trade Commission has effectively removed any incentive for the other primes to seek bids from Aerojet Rocketdyne, the only other provider of SRMs. Although this result may protect prime contractors that, because of the acquisition, feared losing immediate access to NGIS's SRMs, as an unintended consequence the Order will end the competition from Aerojet Rocketdyne that will lead to lower prices and innovation in the future. This is of particular concern as the Department of Defense conducts generational competitions to recapitalize our Nation's strategic defense TRIAD such as the Air Force's Ground Based Strategic Deterrent ("GBSD") program and the Navy's Trident II D-5 submarine launched Fleet ballistic missile follow-on program.

Prior to the merger, all prime contractors would approach both Orbital and Aerojet Rocketdyne to solicit SRM bids. The prime contractors would make their decisions based on the competitive offering from each of the two SRM providers and whether the prime contractor wanted to use both companies, at least partially, to diversify its supplier base.

Post-acquisition, Northrop, when acting as a prime missile system contractor, will supply all of its SRMs from the now vertically-integrated NGIS. Due to the Order, all other primes will simply request that NGIS offer its SRMs at the mandated non-discriminatory terms that Northrop is receiving. This ability will allow other primes to have their supply protected under the Order and therefore eliminate the need to diversify their supplier base. Further, the other primes, when constructing their bids, can communicate to the government or other customers that Northrop has no added benefit from its SRM vertical-integration because all primes are using a virtually identical package from NGIS.

This ability for prime contractors to remove the SRM piece of a bid as a differentiator is highly likely because "[t]he choice of SRM can have a significant impact on the final determination of a missile system prime competition because the propulsion system is a critical element of the overall missile design" and "comprise a large portion of the cost of the integrated missile[.]"[3] Aerojet Rocketdyne's concern is NOT that prices will be too low or that Aerojet Rocketdyne will not be able to provide a competitive offering. The concern is that there will be no more competition due to a regulated SRM offering that NGIS will be required to provide to every prime under the current language of the Order. Thus, competition between Aerojet Rocketdyne and NGIS will be eliminated by the requirements of the Order.

In the long-term, the Order will create one SRM provider. NGIS, already dominant in large SRMs, will now grow increasingly dominant in all SRMs because of the anti-competitive SRM regime put in place by the Order.[4] This lack of competition will reduce innovation and raise prices on all SRMs, even those

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[3] *Id.* at 27777.

[4] *See id.* (June 14, 2018) ("Orbital ATK is one of only two viable suppliers of SRMs for U.S. Government missile systems and the dominant supplier of large SRMs used for long-range strategic missiles.").

unrelated to the GBSD and Trident II D-5 follow-on programs, as the effects on a subset of SRMs have collateral effects on all SRMs. For example, the cost of acquiring the materials necessary in creating any SRM will be affected by changes to the competitive dynamics in only one type of SRM. As the Department of Defense noted, leaving the U.S. with a single SRM supplier will "lead to cost increases due to lack of competition, decreases in internal research and development efforts, and risk of security of supply if a catastrophic accident should occur."[5]

In order to remedy this situation, Aerojet Rocketdyne recommends that the Order's Definition "J" of "Discriminate" or "Discriminating" be modified so that the Order will not be interpreted to create a default to use the SRMs from Northrop's NGIS subsidiary and thereby end all competition in the SRM market.

Aerojet Rocketdyne, which has successfully competed in the SRM market for decades, welcomes the opportunity to compete in the future, and through competition will continue to bring innovative, cost-effective solutions to our Nation's warfighters and NASA. However, it is critical that the Order be modified so that it does not create an SRM regime that eliminates competition in the SRM market. The Order should be modified to foster a competitive SRM market and clarify to all industry participants that the Order has not ended all competition in the SRM market. Aerojet Rocketdyne is willing to further work with the Federal Trade Commission and the Department of Defense to clarify the meaning and intent of the Consent Order so that is does not permit the concerns discussed above.

[5] Office of the Deputy Assistant Secretary of Defense for Manufacturing and Industrial Base Policy, Fiscal Year 2017 Annual Industrial Capabilities at 84 (March 2018).