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UNITED STATES DEPARTMENT OF JUSTICE

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PRESS CONFERENCE REGARDING THE PROPOSED

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LOCKHEED-NORTHROP MERGER

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Conference Room B

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Main Justice Building

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950 Pennsylvania Ave., N.W.

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Washington, D.C.

11

Monday, March 23, 1998

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SPEAKERS:

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HON. JANET RENO, Attorney General of

15

the United States

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HON. WILLIAM S. COHEN, Secretary of Defense

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JOEL I. KLEIN, Assistant Attorney General

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JACQUES GANSLER, PH.D., Under Secretary of

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Defense for Acquisition and Technology

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P R O C E E D I N G S

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(2:00 p.m.)

3

GENERAL RENO: Competition is the lifeblood of a
4 free market economy. It produces better products, more
5 innovation, and lower prices for consumers. This
6 administration's antitrust enforcement policy has been
7 based on a simple principle: In a fast-moving global
8 economy, our nation cannot afford anything less than full-
9 blooded competition.

10

That is why we asked the Federal court in
11 Washington, D.C., today to prevent the merger of the
12 Lockheed Martin Corporation and the Northrop Grumman
13 Corporation, two of the largest suppliers of defense

14 systems to the United States military. This is the single

15 largest merger ever challenged.

16

In our complaint we allege that the proposed

17 merger would substantially reduce competition in many

18 areas of vital importance to America's national defense.

19 It would cost taxpayers more and take the competitive wind

20 out of the sails of innovation in the production of many

21 critical systems that protect our fighting men and women

22 around the world.

23

The defense industry is already highly

24 concentrated. If this merger were to go forward, America

25 could face higher prices and lower quality in advanced

3

1 tactical and strategic aircraft, airborne early warning

2 radar systems, sonar systems, and several types of

3 countermeasure systems that save our pilots from being

4 shot down when they are flying in hostile skies.

5

This merger isn't just about dollars and cents.

6 It's about winning wars and saving lives. That's why the

7 investigation of this merger has been conducted jointly by

8 both the Justice Department and the Department of Defense.

9 Together we want to ensure that any defense merger

10 protects our soldiers' lives and our taxpayers' wallet.

11 Our message is simple: If a merger does not encourage

12 strong competition, it is not in America's interest.

13

Now I'd like to ask Secretary Cohen to say a few

14 words.

15

SECRETARY COHEN: As the principal customer for

16 the products and services of these firms, the Department

17 of Defense has a very significant interest in this

18 proposed acquisition. But before addressing the specifics

19 of the case, I'd like to recount what our policy has been

20 and continues to be regarding mergers and consolidations

21 that have swept the industry in recent years. There are

22 two basic elements to our policy:

23

First, we want to maintain competition for the
24 products and the services that we buy. Going back to the
25 1980's, the early 1980's, I co-authored the Competition in
4
1 Contracting Act, which provided certainly for competition,
2 but numerous other laws as well to promote competition in
3 the Federal acquisition process, and I strongly supported
4 the efforts of several secretaries of defense to adopt
5 acquisition reforms.

6

In defense, as in other industries, competition
7 drives innovation, it improves performance, and it lowers
8 costs.

9

Second, to the extent that a merger does not
10 adversely affect competition, we support consolidations
11 that reduce excess capacity and lower costs to the Defense
12 Department and the American taxpayer. In recent years the
13 Defense Department has worked closely with the Justice
14 Department and the Federal Trade Commission in reviewing

15 mergers and acquisitions in the defense industry,
16 reviewing each proposed transaction on a case by case
17 basis. Also within the Defense Department, we have done
18 significant work in recent years related to the massive
19 mergers that have occurred.

20

We have worked to support consolidations that
21 were in the Department's interests and we have worked to
22 better understand the implications of consolidation in the
23 industry itself. Based on that understanding, we have
24 worked during antitrust reviews to protect the interests
25 of the Department.

5

1

So as this consolidation wave has moved forward,
2 the Department has focused its attention on the problems
3 that could arise from increased vertical integration.
4 During Secretary Bill Perry's tenure, the Defense Science
5 Board was tasked to examine this issue in great detail,
6 and a noteworthy report was released last May by Dr.

7 Kaminski, who was Dr. Perry's acquisition chief and who
8 continued into my tenure. The report highlighted the
9 serious problems that vertical integration could pose in
10 terms of impeding competition and hindering innovation.

11

Firms that are able to produce subsystems or
12 components that go into the products they sell are
13 vertically integrated. Last year's Defense Science Board
14 report, commissioned by Dr. Kaminski, emphasized that
15 vertical integration creates incentives for firms to
16 select subsystems built by their own in-house subsidiaries
17 even when better or cheaper components are available from
18 competitors. It also creates incentives for firms to
19 prevent their subsidiaries from supplying critical
20 knowledge to their competitors. The result is that
21 American soldiers may get inferior products and American
22 taxpayers higher costs.

23

At my very first press conference as Secretary
24 of Defense, I raised the critical importance of preserving
25 competition and the particular concern generated by

6

1 vertical integration. I, along with other senior
2 officials of the Department, including Dr. Gansler, who is
3 here today, have repeatedly raised this issue as being an
4 area of significant concern when we met with leaders of
5 the defense industry.

6

I mention this because such vertical integration
7 problems were an important factor in the Defense
8 Department's review of the proposed Lockheed Martin
9 acquisition of Northrop Grumman, which would bring
10 together two of the four largest contractors.

11

In this specific case -- and again, every case
12 is and must be looked at on its specific merits -- we have
13 conducted a thorough review and concluded that the
14 proposed transaction creates significant problems for
15 maintaining competition. In fact, no previous merger has
16 raised so many interrelated problems, both horizontal and
17 vertical across so many markets. While the problems are

18 numerous, I'd like to focus on just four.

19

First, in the area of electronics, the

20 Department's review concluded that the proposed merger

21 would significantly increase market concentration and

22 adversely affect competition in a number of critical areas

23 of defense electronics. These, as the Attorney General

24 has just mentioned, include electronic warfare, airborne

25 early warning radar, and naval and undersea systems.

7

1

Second, the area of aircraft. The proposed

2 transaction reduces the prospect for innovation and the

3 likelihood of alternative competitive teaming arrangements

4 in aircraft programs. DOD benefits from Northrop

5 Grumman's continued availability to compete or to be a

6 team member for other aircraft programs.

7

Third, in the area of systems engineering and

8 technical assistance. Northrop Grumman assists the

9 Defense Department in managing a number of programs on
10 which Lockheed Martin is either a prime contractor or a
11 bidder. As a result, the proposed merger would create
12 unacceptable conflicts of interest in this area.

13

Finally, the proposed merger creates
14 unprecedented problems of vertical integration. In our
15 judgment, combining Lockheed Martin's strength and
16 platforms and systems with Northrop Grumman's considerable
17 electronics and platform capabilities creates a
18 significant risk to competition at the supplier level.

19

Lockheed Martin and Northrop Grumman are both
20 important suppliers to the Department of Defense and,
21 along with the Department of Justice, we've been in
22 discussion with these companies for some time now to
23 determine whether there were partial remedies that could
24 be addressed -- could address our concerns. We've
25 concluded that the partial remedies proposed by the

8

1 parties pose significant risks and will not resolve the

2 competitive problems by this transaction.

3

I would conclude by noting that our policies
4 have not changed, as some have alleged, but the market is
5 now more concentrated than it was four years ago and
6 mergers therefore require us to exercise greater scrutiny.
7 That said, we intend to continue to review mergers on a
8 case by case basis. We will continue to support mergers
9 that increase efficiencies and do not raise anti-
10 competitive concerns.

11

MR. KLEIN: Thank you, Mr. Secretary, Madam
12 Attorney General.

13

This was a very careful, detailed, and wide-
14 ranging investigation by the Antitrust Division. We
15 worked on this matter cooperatively with the Department of
16 Defense over the last eight months, thoroughly analyzing
17 all the markets that were at stake. Based on that
18 analysis, we concluded that this merger is not in the

19 interest of our nation, its defense efforts, or the
20 taxpayers who will have to foot the bill for that. We
21 want the very best technology for our men and women who
22 serve in the armed forces. The way to get there is to
23 ensure competition. This merger, by contrast, would
24 result in monopolies or near-monopolies on critical
25 technologies that are significant and important to our

9

1 armed forces.

2

The details of our concerns, and they are many,
3 are elaborated in a lengthy complaint that we filed today
4 in Federal district court. In addition, we have the
5 letter from Secretary Cohen amplifying the Department's
6 concerns, and in a moment Dr. Gansler will detail the
7 concerns that we've worked through.

8

I just want to say for our part, this has been a
9 superb cooperative effort between the Department of
10 Defense, who is the principal sole customer for this

11 technology, and the Department of Justice. I am proud and
12 pleased to have worked with them in this important effort,
13 and we will continue to press ahead in the litigation that
14 was filed today.

15

Thank you.

16

MR. GANSLER: As Secretary Cohen said, the
17 decisions we reached in this review were not based on new
18 policies. The policy of maintaining competition and of
19 encouraging the savings that we could get from
20 consolidations where they didn't impact competition is the
21 continued policy we have now and was the policy. What has
22 changed rather dramatically, though, is the environment,
23 and the first chart, if I could have that, gives you a
24 picture.

25

(Chart.)

10

1

2

By the way, we have handouts of these charts for
3 you.

4

This first chart shows pictorially how over the
5 past decade we have essentially gone from about 50 firms
6 listed here -- this is just an example; we didn't list
7 some of the others like General Dynamics and others who
8 still remain. But on this chart alone, we've gone from
9 over 50 firms to 5 for that list. And these aren't small
10 firms, obviously. Looking at the very bottom here, the
11 Northrop Grumman is Westinghouse Electronic Systems Group,
12 Grumman, LTV-Aircraft Operations, these are large firms
13 that have been consolidating as this has taken place.

14

It's this changed environment, as contrasted to
15 any kind of changes in our policy, that has dictated how
16 we look at this current merger.

17

Next slide, please.

18

(Chart.)

19

What we did, both the Justice Department and the
20 Defense Department, separately and exchanging data as we
21 went along, was to take it section by section, in fact
22 program by program, and look at whether or not we were
23 concerned about the implications that took place, and then
24 go back and look at the overall picture.

25

What you see here is the, say, aircraft,

11

1 horizontal and then vertical implications. The red areas
2 are those areas in which as a result of the merger there
3 was essentially a move towards a monopoly situation. In
4 other words, there were two people in the industry, such
5 as for an example in airborne early warning radar systems,
6 the two remaining players would effectively have become
7 one player, a move towards monopoly.

8

In other cases, there was a considerable

9 consolidation. We show that as the orange or yellow color
10 shown there, where there still was some competition left,
11 but it was down to perhaps going from three to two.

12

In the case of the white, that doesn't mean that
13 there was not a concern on our part. For example, in the
14 case of the radar systems it just simply means that there
15 were still no impacts as a result of the merger that took
16 place. In other words, there may have been two, in this
17 case Raytheon and Northrop were the two radar suppliers,
18 but they're still there after the merger, so it had no
19 impact even though it was still a limited number of
20 suppliers.

21

As you can see, in the vertical case there were
22 some significant impacts even in cases where we had no
23 impact as a result of the merger in the case of the
24 radars.

25

It's the overall impression, then, that one gets

12

1 in looking at this chart that shows why Secretary Cohen
2 said that this had such a significant impact across the
3 board in terms of both vertical and horizontal impacts.

4 And should you want to, we can go into this in more detail
5 later on.

6

Next slide, please.

7

(Chart.)

8

Lastly, to pictorially show the vertical
9 integration issue, we've shown here -- in the case of
10 aircraft this one was; we could do the same for ships, but
11 this is the Lockheed Martin areas in which they have
12 significant capability, the areas where Northrop Grumman
13 has significant capability in terms of aircraft. And as
14 you can see, the difference here between, for example, the
15 Boeing case, where Boeing and McDonnell Douglas were
16 merged, it didn't create the vertical issues that we see
17 in the case of Northrop Grumman and Lockheed Martin.

18 These are the two vertically integrated corporations which
19 would then be combined in that situation.

20

The same thing you can see again for Raytheon.

21 They're, of course, not in the aircraft, the military
22 aircraft business, so you don't see that situation.

23

It's effectively the combination of these three
24 charts, the change in the environment, the impact in the
25 horizontal and vertical case across the board, that leads

13

1 us to making the decision that we're making today.

2

Thank you.

3

MR. KLEIN: At this point the Attorney General
4 and the Secretary have other commitments. Dr. Gansler and
5 I would be prepared to answer your questions.

6

QUESTION: The industry says that there's a

7 considerable element of unfairness in the way this all
8 unfolded, that you essentially sucker punched them on that
9 March 6th meeting with Kent Chris and all his executives;
10 that all these speeches about vertical integration did not
11 substitute for adequate detailed warnings.

12

Can you address that issue, both of you?

13

MR. KLEIN: Yes. Let me say I think we
14 conducted this investigation the way we conduct all our
15 investigations. We analyzed the material, put the parties
16 on notice as to what our concerns were, and throughout the
17 process they knew that all of the issues that we are
18 currently suing on were in play, of significant concern,
19 and as the process moved forward they had every reason to
20 believe that this merger was running into substantial
21 trouble.

22

Now, the details of that and the negotiations
23 that we had, I have a complete chronology and, if the
24 parties are prepared to waive their confidentiality of

25 those communications, I would be glad to give you a day by

14

1 day tick-tock with respect to these issues. But I can

2 assure you that we were upfront and forthcoming, as we are

3 in our processes, in telling them what the concerns were,

4 where the problems were, and the magnitude of those

5 problems.

6

QUESTION: There's reports this morning that say

7 that the divestiture is the key issue, that if both sides

8 were willing to divest up to \$4 billion worth of their

9 companies that that would no longer be a problem for the

10 Justice Department. Is that true? And secondarily, if

11 they were to divest up to that amount of money, would you

12 consider dropping this suit?

13

MR. KLEIN: I'm not going to negotiate in public

14 with respect to these matters. We believe this merger

15 should be blocked. Whether there is a remedy short of

16 that, none has been put forward by the parties at this

17 point. We would obviously entertain any such proposal in
18 conjunction with the Department of Defense.

19

At this point there is nothing on the table that
20 would satisfy the concerns that have been raised.

21

QUESTION: I have a question for Dr. Gansler.

22 Where do you expect Northrop to go now? Do you expect
23 them to remain standing alone as an \$8 billion company in
24 an environment of \$40 billion companies? Or do you expect
25 them to merger with someone else? And that raises the

15

1 question, are your remedies worse than the probably you're
2 trying to address?

3

MR. GANSLER: Well, let me first comment on the
4 fact that there's no question in our minds or in the minds
5 of Northrop that they are a viable corporation as they
6 exist now in terms of their profit, their sales for the
7 foreseeable future over the next at least five or six

8 years that we looked at in detail. Beyond that, of
9 course, it's hard to tell. But they have the strength in
10 the aircraft subsystems, they have a leadership position
11 in the stealth technology. They are certainly leaders in
12 many of the electronics areas that I covered on the chart,
13 and they are a very viable corporation, there's no
14 question in our minds, as they exist now.

15

They may well choose -- and that's their
16 corporate policy, and they had announced it earlier that
17 they might choose to make additional acquisitions, and
18 that would be up to them. We would assess those in the
19 same way we have assessed this one and the prior ones,
20 namely what's the impact on competition and what's the
21 impact on potential savings, and we'd assess it that way
22 from our viewpoint. What they do is of course up to them.

23

QUESTION: Are you confident that your remedy is
24 better than the problem that you're addressing?

25

MR. GANSLER: Yes, definitely.

16

1

MR. KLEIN: Ron.

2

3

QUESTION: Mr. Klein, given the language of the
4 letter of the Secretary of Defense here, "We have also
5 concluded that partial solutions addressing individual
6 competitive issues will not be adequate," that sounds more
7 like something greater than nothing's on the table. That
8 sounds like nothing could ever be on the table. Isn't
9 that a flat rejection of any possibility of a settlement?

10

MR. KLEIN: Again, Ron, I don't think it's
11 appropriate to negotiate in public. They understand the
12 various concerns that have been articulated, the possible
13 remedies that might be acceptable, and if they want to
14 come forward with such then the Department of Defense and
15 the Department of Justice would surely analyze those.

16

QUESTION: There's a sense, Mr. Klein, around
17 town that DOJ -- that you and the Pentagon really never
18 wanted this merger to go forward to begin with, that you
19 raised the bar so high and made it so unattractive for the
20 parties to complete the merger that it was just a policy
21 decision that you didn't want this to happen, period.

22

MR. KLEIN: It's not a question of wanting it to
23 happen or not. The question which we go through, and I
24 think in this case cooperatively with DOD, is what is the
25 impact of this merger on various markets? And by any

17

1 conventional antitrust analysis, the level of
2 consolidation that permeates this is huge.

3

We didn't make a policy decision, we didn't go
4 through an eight-month investigation of millions of
5 documents and take depositions of lots of witnesses to
6 come to a foregone conclusion. We did the analysis, we
7 kept them apprised of the work that we are doing. When we

8 saw the competitive problems, we actually engaged them in
9 discussions about solutions, solutions that they
10 ultimately appear to find unacceptable.

11

But in any event, our commitment is to enforce
12 the antitrust laws. Short of a solution that would fully
13 protect America and its military needs in this market, we
14 would not entertain it.

15

QUESTION: But do you see their point of view in
16 the sense of, if you force them to spin off the crown
17 jewel, the electronics division and everything else, \$4
18 billion worth of property, what's the point of doing the
19 merger?

20

MR. KLEIN: Well, but that's a question that you
21 can only direct to them. From our point of view, the
22 point is to enforce the antitrust laws, and any merger
23 where we conclude that it will harm competition, hurt
24 America's consumers, we enforce them.

25

The parties made a business judgment as to how

18

1 to proceed and it's not our job to second guess that

2 business judgment. Our job is to enforce the law.

3

QUESTION: Dr. Gansler, all this is a bit,

4 probably a bit complicated for the average American

5 taxpayer. Can you take one system, one vital system, and

6 show how the acquisition of this system will be affected

7 if this merger was allowed to go through?

8

MR. GANSLER: Well, one of the examples that was

9 given by both the Attorney General and the Secretary was

10 airborne early warning radar systems. There there are two

11 suppliers currently, Lockheed and Northrop. As a result

12 of the merger there would be one supplier. There's ample

13 evidence that monopolies tend not to go towards innovation

14 or low cost, so that's the rationale.

15

I think in many of those areas where the merger

16 resulted in going from two to one, that's not really a
17 question of dispute in terms of the impact on the
18 companies.

19

QUESTION: So you think you'd have an inferior
20 early warning radar system if this merger were to --

21

MR. GANSLER: Over time. We would have
22 eliminated the opportunities for innovation and
23 competition and the benefits that would come from
24 competition.

25

QUESTION: Here in the back. Mr. Klein, if this
19
1 were to actually be litigated, could you give us some kind
2 of sense of what the shortest time frame versus what the
3 longest time frame is that it would actually reach some
4 sort of legal conclusion?

5

MR. KLEIN: Well, again it's hard for me. It's

6 a schedule the judge would set, but I would say as
7 follows. At least as I understand it, the parties have
8 not yet decided to close and announced they wouldn't
9 attempt to close before April 24th. At some point I
10 presume, if the case is litigated, they will set, the
11 judge will set a schedule for a preliminary injunction
12 hearing, which could take several months certainly before
13 the court would set that matter for hearing. And I would
14 imagine that a good deal of the litigation would take
15 place at the preliminary injunction stage.

16

QUESTION: And that would be concluded by this
17 year?

18

MR. KLEIN: Again, the schedule is up to the
19 judge. If you look at the past, for example, you know as
20 well as I what the schedule was in the recent Staples
21 case, which was litigated here in the District of
22 Columbia, and we filed this case as well in the Federal
23 District Court here in the District of Columbia. That's
24 probably as good a guess as anyone could give you right

25 now.

20

1

QUESTION: Is this a message to Lockheed Martin
2 that the growth that they've experienced in their defense
3 electronics is at a peak, that they can't do more
4 acquisitions in that particular area because it would be
5 too great a concentration vertically?

6

MR. KLEIN: I don't think there's a question of
7 sending any messages. I think any acquisition has to be
8 evaluated on its own merits. When we evaluated, along
9 with the Department of Defense, the Raytheon-Texas
10 Instruments merger, we required a substantial divestiture
11 of MIMICS. That was because that's where the competitive
12 problem was.

13

In this one we think the competitive problems
14 are pervasive. In another merger, we would do the work
15 and do the analysis, and if there were no probably

16 obviously we would not contest it.

17

QUESTION: Two questions. One is, this morning
18 Lockheed indicated that they had given some sort of
19 proposal to you over the weekend. What was the -- if you
20 could just tell us what that proposal was? Obviously, it
21 fell short.

22

And then secondly, what are the implications of
23 this for potential mergers among second tier defense
24 contractors?

25

MR. KLEIN: Again, as to the proposal, I really
21
1 think it is not the way we do business, and indeed not the
2 way settlement discussions are supposed to take place
3 under the Federal Rules. So I'm not going to disclose it.
4 They are obviously free to.

5

In terms of other defense mergers, once again I

6 think Secretary Cohen certainly said that this is not
7 meant to mean that all mergers should come to a screeching
8 halt. I think you have to look at the product markets
9 that are affected by it and you have to look as well at
10 the efficiencies.

11

But I would suggest to you, when you're looking
12 at a larger number of two to one mergers where you're also
13 talking about the people who have the key platform, here
14 the aircraft platform, merging as well, the amount of
15 vertical and horizontal problems can be very, very
16 significant. In other instances those problems might well
17 not arise.

18

Go ahead, Dick.

19

QUESTION: Secretary Cohen also said in his
20 letter to Ms. Reno that the problems here "are an
21 outgrowth of the significant consolidation in the defense
22 industry that has taken place in recent years." As there
23 is fewer and fewer musical chairs, isn't it simply going

24 to be harder and harder for almost any merger to take

25 place?

22

1

MR. KLEIN: Well, I think certainly, as you

2 probably recall, last July when I was testifying before

3 the Antitrust Subcommittee on just these set of issues, we

4 did indicate that obviously as you get fewer and fewer

5 players the vertical issues become more important. In

6 general, if you had a significant number of primary

7 contractors and secondary contractors, vertical issues

8 would be less important.

9

But none of that is to foreclose the specifics

10 of any given case, and if they don't raise competitive

11 concerns and they are pro-competitive we certainly would

12 support them.

13

QUESTION: One of the other arguments you hear

14 out of industry is that there are already examples of

15 types of equipment that are already supplied only by a
16 single company, like armored vehicles or some of the
17 submarine technology. If that's true, then how can you -
18 - how do you distinguish where it's okay to have a single
19 supplier and where it's not? You don't think that's true?
20

MR. KLEIN: Let me say a quick word and then I
21 think Jacques.
22

From my point of view, that's exactly why we do
23 the analysis. You have to really understand the market,
24 understand the technologies and capabilities of potential
25 players, understand how easy or difficult it would be for
23
1 a new entrant to come into that market who may be in an
2 adjacent market, understand what the military's needs are
3 going to be. How likely are we going to see a contract
4 that's bid?
5

All of that is the detailed work that we've done

6 over the past eight months. So there are no simple
7 analogies to other products and other markets. It doesn't
8 work that way.

9

MR. GANSLER: There may be many areas where you
10 have only a single supplier. That doesn't mean that other
11 people couldn't come into that market with different
12 technologies or different ways to solve the mission
13 problem, as contrasted to currently we have a single
14 supplier of a single product.

15

The defense industry is responding to a market
16 that is very lumpy. You know, we do very few
17 procurements, they're very infrequent, and so many, many
18 times you'll have only a single supplier. But as long as
19 there's the potential for other people to enter into that
20 market without very huge investments and very long time
21 periods, then that's an acceptable situation.

22

In many of these cases that we went through, we
23 in fact would result in taking a very, very large

24 investment to bring someone back into that market and a
25 very long time period, and that's an unacceptable
24
1 solution.

2

QUESTION: Dr. Gansler, the Secretary and you
3 named some instances of particular products and areas,
4 electronics and aircraft and so on, and then went on to
5 say something about the one company being a contractor,
6 the other a subcontractor, would go out the window. The
7 latter makes it sound like anything that these companies
8 did to merge would obviously cause a roadblock there.

9

Would you go into this dichotomy?

10

MR. GANSLER: There are some products that are
11 absolutely critical. If you were to have, say, a next
12 generation fighter plane, you'd have to have radars, you'd
13 have to have electronic countermeasures. Some of these
14 systems are the essence of next generation systems, and

15 it's in those areas where you worry about vertical

16 integration.

17

There are many other products that one could

18 have on an aircraft that probably wouldn't be the major

19 differentiators in those product areas. So we limited

20 ourselves in the analysis to those critical subsystems and

21 those areas where there would in fact be a great

22 diminution of competition.

23

QUESTION: Mr. Klein, in one of your previous

24 answers you left the door open to further negotiations

25 with the companies to try and reach some kind of

25

1 settlement. But given whatever their most recent

2 proposals were, what's the likelihood of you being able to

3 reach a settlement with them on this? Would you say that

4 by the time you made the decision there was a wide gap

5 between what you wanted and what the company wanted, or is

6 there a small gap? Is it bridgeable or what?

7

MR. KLEIN: I think there's a significant gap,
8 certainly is why we decided to go to court. They have
9 known what our concerns are and we've talked openly about
10 them with the parties. They have not been able to meet
11 those concerns, and so we decided now is the time to
12 proceed to litigation.

13

QUESTION: But you don't rule out further
14 settlement talks at some point?

15

MR. KLEIN: I never -- and our practice has
16 been, we have filed lawsuits and subsequently settled
17 them. I will not rule it out in this instance.

18

In the back.

19

QUESTION: Two questions. In the Loral deal
20 there were some monopolies created, I believe anti-
21 submarine warfare, and vertical integration was a very
22 large issue there. How is that different from this?

23

The second question is, some people are

24 suggesting if you give contracts to systems integrators,

25 who then pick the platform and the subsystems, it would be

26

1 a solution short of this, a change in procurement

2 procedure, that would preserve competition. Is that a

3 viable option in the future?

4

MR. GANSLER: First of all, the Loral case was

5 in fact the one that caused the Defense Science Board

6 study that Secretary Cohen mentioned to be done in terms

7 of vertical integration. So it did raise concerns. We

8 did have an outside group look at it. We did a lot of

9 analysis in that case, the same way we did in this case,

10 and concluded that that would be acceptable, but raised

11 the concerns that we, all four of us, have said in terms

12 of the continuing influence of the closing environment,

13 with the number of firms being reduced significantly and

14 thus causing us to continue to look even more carefully at

15 the vertical integration question.

16

Your second question?

17

QUESTION: Awarding contracts to a systems

18 integrator as opposed to a platform?

19

MR. GANSLER: There are a variety of different

20 approaches that one could take to try to address the

21 vertical integration question. One would be awarding

22 contracts to a systems integrator. Another would be for

23 the government to play the role of the systems integrator,

24 which historically we often did in the past. Another one

25 would be for the government to start buying government-

27

1 furnished equipment, in other words buy the radars

2 directly, buy the computers, buy the airplane, do all the

3 integration ourselves.

4

As a result of the acquisition reform

5 initiatives that we've been taking over the last few
6 years, we've been moving in the other direction. We've
7 been moving in the direction of trying to have the prime
8 contractor do the systems integration, of having the prime
9 contractors establish their competitive teams for the
10 competitions, and of having the government back off from
11 supplying the equipment or getting involved in the
12 regulation of the industry structure in terms of make-buy
13 decisions or vertical integration.

14

We've also been shrinking the number of people
15 in the acquisition work force. In the defense acquisition
16 work force from 1989 to 1997, we've actually reduced the
17 work force by about 42 percent. So it's all consistent in
18 terms of our strategy. It's to have less people and count
19 much more on the systems integration being done by the
20 prime contractors, so that any vertical integration move
21 would be contrary to that. And we don't want to get
22 ourselves in the middle of trying to make make-buy
23 decisions associated with a company.

24

In other words, you have two choices in
25 addressing vertical integration. You can do it
28
1 structurally or you can do it with a regulatory approach.
2 We're trying to move away from regulation, going more
3 towards commercial buying practices and commercial
4 practices across the board. And we feel that that would
5 be inconsistent, for us to go in the direction of more
6 regulation over, say, make-buy decisions or vertical
7 integration of the companies.

8

MR. KLEIN: Ann Marie.

9

QUESTION: It sounds from the complaint like you
10 have gotten hold of some company documents that imply that
11 they were trying to merger to eliminate competition. Is
12 there a lot of that in this case?

13

Don't laugh at me.

14

MR. KLEIN: The complaint will have to speak for
15 itself, obviously. I can't disclose the evidence that we
16 have beyond what's in the complaint at this point.

17

Go ahead.

18

QUESTION: You mentioned you're looking at
19 monopolies in terms of down the road. Are you factoring
20 in the possibility of buying from non-American companies
21 in the future as an answer to competition?

22

MR. GANSLER: In looking at the potential
23 sources for most of this critical defense equipment,
24 because we haven't in terms of major subsystems or major
25 systems bought much offshore, that's a lower probability
29
1 of them entering into the market. We have been
2 encouraging over the last few years more cooperative
3 development and more trans-Atlantic and trans-Pacific co-
4 developments and coproduction programs.

5

But in general, in these areas that we're
6 talking about here the U.S. tends to be the leader in
7 those fields, and so there really aren't viable
8 international sources for most of these critical things we
9 are talking about.

10

MR. KLEIN: All right, we'll take one more. Go
11 ahead.

12

QUESTION: Can you tell us what you asked them
13 to divest? Was it actually \$4 billion worth of
14 electronics business?

15

MR. KLEIN: Again, I just think it's not
16 appropriate for us to negotiate. They know what it was
17 that we asked and they are free, of course, to disclose
18 what they feel comfortable with.

19

All right, thank you all very much.

20

(Whereupon, at 2:33 p.m., the press conference

21 was concluded.)

22

23

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25