IN THE UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF ILLINOIS
ROCK ISLAND DIVISION

UNITED STATES OF AMERICA, Plaintiff, v. ALLIANT TECHSYSTEMS INC. and AEROJET-GENERAL CORPORATION, Defendants.	Civ. No. 94-1026 Filed: 1/19/94 COMPETITIVE IMPACT STATEMENT

Pursuant to Section 2(b) of the Antitrust Procedures and Penalties Act, 15 U.S.C. § 16(b)-(h), the United States submits this Competitive Impact Statement relating to the proposed Final Judgment that is being simultaneously lodged with the consent of Alliant Techsystems Inc. ("Alliant") and Aerojet-General Corporation ("Aerojet") in this civil antitrust proceeding.

I.

NATURE AND PURPOSE OF THE PROCEEDING

On January 19, 1994, the United States filed a civil antitrust complaint alleging that Alliant and Aerojet entered into a teaming arrangement suppressing and eliminating competition between them in violation of Section 1 of the Sherman Act, 15 U.S.C. § 1. The Complaint seeks both monetary and equitable relief.

The Complaint alleges that beginning in or about August 1992, the defendants have engaged in a continuing agreement, combination and conspiracy to suppress and eliminate competition in the

production and sale to the United States of Combined Effects Munition ("CEM") systems, which are a type of cluster bomb. In response to a formal Government solicitation for competitive proposals in 1992 for the supply of such CEM systems, the defendants, instead of submitting independent competitive proposals as requested, entered into a teaming arrangement, the purpose and effect of which was (a) to eliminate competitive bidding between them, and (b) to divide between them, as equally as possible, the production, revenue, and profit from the anticipated procurement.

Under the arrangement, Alliant was to act as prime contractor, and Aerojet, in consideration of its not submitting a competitive bid, would receive from Alliant a subcontract for certain designated components of CEM systems. The effect of the arrangement was to reduce the number of bidders from two to one on the 1992 procurement and to substantially raise the price of the single offer that defendants submitted. By its terms, the arrangement was also to apply to future procurements beyond the 1992 solicitation of CEM systems.

The Complaint seeks a payment of money as relief in connection with the 1992 procurement and an injunction prohibiting the continuation of this or any similar arrangement on future competitive procurements of CEM systems by the United States.

On January 19, 1994, the United States, Alliant and Aerojet filed a Stipulation in which they consented to the entry of the proposed Final Judgment requiring them to make payments to the

United States and prohibiting certain conduct. The defendants will also be required to institute a compliance program to ensure that they do not continue or renew the teaming arrangement or engage in any other agreement, contract, combination, or conspiracy having a similar purpose or effect in response to requests or invitations by the United States or any United States agency for competitive offers, quotations, bids or proposals. Additionally, the proposed Final Judgment requires that Alliant and Aerojet file annual reports with the Government certifying that each has complied with Section VI of the Final Judgment. The proposed Final Judgment will provide the relief the United States seeks in the Complaint.

The United States and the defendants have stipulated that the Court may enter the proposed Final Judgment after compliance with the Antitrust Procedures and Penalties Act, 15 U.S.C. § 16, provided the United States has not withdrawn its consent. The proposed Final Judgment provides that its entry does not constitute any evidence against or admission by any party with respect to any issue of fact or law.

Entry of the proposed Final Judgment will terminate the action against Alliant and Aerojet, except that the Court will retain jurisdiction over the matter for further proceedings that may be required to interpret, enforce, or modify the Final Judgment, or to punish violations of any of its provisions.

II.

DESCRIPTION OF THE PRACTICES INVOLVED IN THE ALLEGED VIOLATIONS

A. Industry Background

The relevant product is a CEM system. A CEM system is a type of "cluster bomb." The CEM system is technologically the most modern cluster bomb in current production for the United States military. However, it is not a "smart" bomb. The main bomb body contains a cluster of approximately 200 bomblets that spread out in mid-air after the bomb is dropped from aircraft. The bomblets, which have anti-personnel, anti-armor, and incendiary capabilities, explode on impact. The United States Air Force used the CEM system extensively in Operation Desert Storm.

Aerojet initially developed the CEM system for the Air Force under contracts awarded in 1974 and 1979. The Air Force awarded the first production contract to Aerojet in 1983.

In the mid-1980's, the Air Force adopted a CEM procurement strategy that called for having a second source for CEM production, in addition to Aerojet. The dual source approach was designed to secure the benefits of competition for future procurement and to expand the CEM industrial base. The Air Force awarded a second-source contract to Honeywell, Inc. The division of Honeywell responsible for production of CEM systems was later spun off as Alliant.

In operation, the procurement strategy contemplated an award of some quantity of CEM systems to each of the two competitors

each year. The low bidder received the larger production award. The relative quantities awarded were determined by a formula that took into account the magnitude of the difference in the prices of the two bids. The strategy permitted a winner-take-all award, sometimes called a "competitive downselect," to the low bidder in the final year of the program. Such a competitive downselect would maximize cost savings to the Government when two producers were no longer necessary.

Since 1987, all the requirements of the United States military for CEM systems have been procured by the United States Army Armament, Munitions and Chemical Command ("AMCCOM") in Rock Island, Illinois. This procurement has been pursuant to AMCCOM's mission as the Department of Defense ("DOD") Single Manager for Conventional Ammunition. AMCCOM has continued the dual-source procurement strategy initiated by the Air Force.

B. Illegal Teaming Arrangement To Eliminate Competition, Raise Price, And Divide Production

After separate negotiated awards to Aerojet and Alliant's predecessor (Honeywell) in 1985, the Air Force and then AMCCOM annually solicited independent and competitive proposals from the two sources, Alliant (including its predecessor) and Aerojet. Through 1991, Alliant and Aerojet each annually submitted and certified the independence of competitive offers. From 1985 through 1991, the Department of Defense acquired approximately $1.75 billion in CEM systems from the two defense contractors.

During the period of competitive procurement, the price the Government paid for CEM systems declined significantly. From 1986 to 1989, the price declined an average of 20% each year. A competitive downselect in 1990 resulted in the lowest price ever. In 1991, following renewal of the program to replenish inventories depleted by Operation Desert Storm, AMCCOM returned to the dual-source award strategy. The 1991 prices were somewhat higher than in 1990.

In the summer of 1992, there was a second competitive solicitation to replenish inventories depleted by Operation Desert Storm. In response, instead of submitting separate offers, as they had in each of the previous six years, Alliant and Aerojet entered into a teaming arrangement to submit only a single offer. Under the written teaming arrangement, Alliant was to act as the prime contractor and Aerojet as a subcontractor. The production of CEM systems was to be divided equally between the two companies, with each supplying certain designated components of the system. Under the arrangement, Aerojet was not to submit a bid as a prime contractor. Accordingly, there would be no competition between the only two companies qualified to provide CEM systems to the United States. The teaming arrangement was to apply to all U.S. procurement of CEM systems, for 1992 and beyond. Although there was no 1993 procurement of CEM systems, at this point it appears that there will be a 1994 procurement.

The Government did not approve or accept the teaming arrangement. Upon receipt of the single offer, at a price

significantly higher than in the past, AMCCOM did not make an award at a firm, fixed price, as originally contemplated. Rather, AMCCOM awarded production as an "undefinitized contract action." This form of award accepted the bid price as a ceiling only, with AMCCOM retaining the right to negotiate the price downward, and, if necessary, make a unilateral price determination. Under the Federal Acquisition Regulations, any unilateral price determination is subject to contractor recourse to a claims process intended to ensure establishment of a "fair and reasonable" price. The award as an undefinitized contract action was justified by an urgent, documented national security need for uninterrupted CEM production. Continuous production was urgently needed to keep the CEM industrial base "warm" and to avoid significant costs of start-up that would be required in the event of a production interruption.

By two other steps, AMCCOM formally made clear that it did not approve or accept the teaming arrangement. First, in the notice of contract award to Alliant, AMCCOM expressly stated that the award did not constitute acceptance or approval of the teaming arrangement. Second, AMCCOM, through the Army's Office of General Counsel, referred the matter to the Department of Justice for investigation of the teaming arrangement as a possible antitrust violation.

Although Alliant and Aerojet disclosed their intention to enter into a teaming arrangement in advance to AMCCOM, this disclosure did not create, and could not have created, antitrust

immunity for the teaming arrangement. Department of Defense personnel are not authorized, and it is not their role under the Federal Acquisition Regulations or applicable case law, to give antitrust clearance to teaming arrangements.

The teaming arrangement had the effect of raising the price of the single offer for 1992 CEM production that the team presented to AMCCOM. The teaming arrangement also had the effect of increasing, above historical levels, the costs and profits that the prime contractor claimed as fair and reasonable under the undefinitized contract action.

III.

EXPLANATION OF THE PROPOSED FINAL JUDGMENT

The proposed Final Judgment is part of a broader settlement that has two aspects. One aspect is a net savings of about $12 million from the price the Alliant/Aerojet team originally offered in response to AMCCOM's solicitation of competitive proposals for the 1992 CEM procurement. The $12 million in savings will be realized as follows. First, the defendants will make payments of about $4 million to the United States under the proposed Final Judgment. Second, as settlement of the Undefinitized Contract Action for the 1992 CEM procurement, AMCCOM will pay Alliant, the prime contractor, about $8 million less than the team's bid price.

The second aspect of the broader settlement is the prohibited conduct in the proposed Final Judgment. This injunctive language is intended to ensure that Alliant and Aerojet not continue or renew their teaming arrangement for future procurements of CEM systems in which the United States solicits competition.

The Department of Justice believes that the proposed Final Judgment combined with the negotiated reduction of the contract price contains provisions sufficient to remedy the effects of the teaming arrangement on the 1992 CEM procurement and to prevent further violations by Alliant and Aerojet of the type alleged in the Complaint.

A. Financial Terms

Section V of the proposed Final Judgment would require Alliant and Aerojet to make payments to the United States, delivered to the Antitrust Division of the Department of Justice, which will, in turn, forward these receipts to the appropriate military account for CEM system procurement. Each defendant is to pay $2.0475 million plus interest from the date of entry of the Final Judgment; the combined total payments will be $4.095 million, plus interest. These payments by Alliant and Aerojet are intended to be refunds to the appropriations of the United States for CEM procurement.

The broader settlement also includes agreement on a contract price of $125.775 million for the 1992 CEM procurement. This price constitutes about an $8 million reduction from the team's original bid price of approximately $133.7 million in September 1992. This $8 million price reduction is not part of the proposed Final Judgment, but is to be formalized in a separate contract modification agreement between AMCCOM and Alliant. Upon execution of the formal contract modification, which is planned contemporaneously with the parties' agreement to the proposed

Final Judgment, the relevant portions of the modification will be lodged with the Court to be available for public inspection.

The net price paid by the Government for the 1992 CEM procurement under the settlement will be $121.68 million -- the $125.775 million negotiated contract price minus the $4.095 million refund paid directly to the United States.

The actual amount that the low bidder would have proposed to AMCCOM for the 1992 CEM procurement in the absence of the teaming arrangement is not readily provable. The net price of $121.68 million that the Government is to pay under this settlement is the best approximation that can be made of what competition would have produced. The $12 million price decrease represents about 10% of the final price of $121.68 million. For comparison, the Sentencing Guidelines for criminal violations of Section 1 of the Sherman Act estimate that the average gain from price fixing is 10% of the selling price. United States Sentencing Commission, Guidelines Manual, § 2R1.1, comment, n. 3 (Nov. 1992).

B. Prohibited Conduct

Section IV of the proposed Final Judgment would enjoin future teaming between Alliant and Aerojet to supply CEM systems to the United States, unless the Justice Department or the Court approves the teaming in advance. This explicit prior approval requirement is intended as a remedial measure to assure that neither Alliant nor Aerojet misuse teaming arrangements to suppress competition.

The prior approval requirement in the proposed Final Judgment will emphasize to the defense community generally that the Federal Acquisition Regulations do not confer antitrust immunity. Subpart 9.602 of the Federal Acquisition Regulations states the general policy that the Government recognizes the integrity and validity of teaming arrangements, if disclosed in advance; however, Subpart 9.604 explicitly provides that the general policy does not confer antitrust immunity on teaming arrangements. It is the responsibility of the Justice Department, and not other components of the Executive Branch, to make statements of federal enforcement intention with regard to possible violations of Section 1 of the Sherman Act. The Antitrust Division of the Department of Justice has a Business Review procedure in place that is available, when the requirements of the procedure are met, to provide statements of enforcement intention with regard to proposed business conduct.

The proposed Final Judgment would not limit the flexibility of the Department of Defense in procuring CEM systems. The Defense Department retains all the CEM acquisition options provided by the Federal Acquisition Regulations. The prohibition in the Final Judgment on teaming relates only to those CEM acquisitions for which the procurement office has determined that it is appropriate to solicit competition.

By prohibiting further CEM teaming, the proposed Final Judgment would enable the competitive procurement process to resume. Where procurement through competition is an available and practical option, it allows the Government to avoid the

administrative expense of negotiating prices and to efficiently obtain price and quality benefits. In the absence of competition, AMCCOM must attempt to negotiate a fair and reasonable price. These negotiations can be time-consuming and costly to the Government, costing hundreds of thousands of dollars each year.

The proposed Final Judgment also would permit subcontracting between Alliant and Aerojet, so long as the purpose or effect of the subcontracting is not to eliminate or suppress competition in the supply of CEM systems to the United States. In some instances such subcontracting may be the most efficient way of supplying particular CEM system components to the Government. Accordingly, permitting such subcontracting could reduce the United States' CEM procurement costs.

C. Compliance Program And Certification

In addition to the prohibitions contained in Section IV of the Proposed Final Judgment, Alliant and Aerojet each would be required to implement an antitrust compliance program. As part of the program, each defendant would distribute copies of the Final Judgment to all officers of that defendant, to the employees who are responsible for executing Certificates of Independent Price Determination for CEM system procurement, and to those employees who are principally involved in determining the company's bid for such procurements. These persons would be required to annually certify that they understand and agree to abide by the terms of the Final Judgment.

D. Applicability To Successors And Assigns

Section III of the proposed Final Judgment makes the Final Judgment applicable to the successors and assigns of each defendant. Each defendant must require, as a condition of the sale of its assets used in the production of CEM systems, that the buyer agree to be bound by the provisions of the Final Judgment. At the time of lodging of the proposed Final Judgment with the Court, the United States was aware that a sale to Olin Corporation by Aerojet of its CEM production assets in Downey and Chico, California had been discussed. The Stipulation Re Entry of Final Judgment, which the parties have lodged with the Court, provides that Alliant and Aerojet, from the time of filing of the Stipulation, shall comply with the terms of the proposed Final Judgment as if these terms had been ordered by the Court. Section III of the proposed Final Judgment, which addresses successors and assigns and the sale of CEM assets, in combination with this provision of the Stipulation, is intended to ensure that before Aerojet consummates any sale of its CEM business, it requires the purchaser to agree to be bound by the provisions of the proposed Final Judgment.

E. Effect Of The Proposed Final Judgment On Competition

The relief in the proposed Final Judgment is designed to prevent Alliant and Aerojet from continuing or renewing their teaming conduct that has suppressed and restrained competition in the supply of CEM systems. It is also intended to remedy the price impact of the teaming arrangement on the 1992 CEM procurement. The Department of Justice believes that the proposed

Final Judgment contains sufficient provisions to prevent further violations by Alliant and Aerojet and, in combination with the negotiated reduction in the contract price for the 1992 CEM procurement, to remedy the price impact of the teaming on the 1992 procurement.

IV.

REMEDIES AVAILABLE TO POTENTIAL PRIVATE LITIGANTS

Section 4 of the Clayton Act, 15 U.S.C. § 15, provides that any person who has been injured as a result of conduct prohibited by the antitrust laws may bring suit in federal court to recover three times the damages suffered, as well as costs and reasonable attorney's fees. Entry of the proposed Final Judgment will neither impair nor assist the bringing of such actions. Under the provisions of Section 5(a) of the Clayton Act, 15 U.S.C. § 16(a), the Final Judgment has no prima facie effect in any subsequent lawsuits that may be brought against any defendant in this matter.

V.

PROCEDURES AVAILABLE FOR MODIFICATION OF THE PROPOSED FINAL JUDGMENT

As provided by the Antitrust Procedures and Penalties Act, any person believing that the proposed Final Judgment should be modified may submit written comments to Gary R. Spratling, Chief, Antitrust Division, U.S. Department of Justice, 450 Golden Gate Avenue, Box 36046, San Francisco, CA 94102, within the 60-day period provided by the Act. These comments, and the Department's

responses, will be filed with the Court and published in the Federal Register. All comments will be given due consideration by the Department of Justice, which remains free to withdraw its consent to the proposed Final Judgment at any time prior to entry. In addition, the proposed Final Judgment provides that the Court retains jurisdiction over this action, and the parties may apply to the Court for any order necessary or appropriate for the modification, interpretation or enforcement of the Final Judgment.

VI.

ALTERNATIVES TO THE PROPOSED FINAL JUDGMENT

As an alternative to the proposed Final Judgment, the Department of Justice could have recommended that AMCCOM attempt to negotiate a lower contract price for the 1992 CEM procurement pursuant to the Undefinitized Contract Action. Such a form of settlement, avoiding payments explicitly as relief for an antitrust violation, could have minimized publicity adverse to Alliant and Aerojet about the price impact of their illegal conduct. In the view of the Department of Justice, such a form of relief, in the absence of very significant public financial benefits, is unwarranted and contrary to the public interest in general deterrence that is served by the form of settlement used.

Another alternative to the proposed Final Judgment would be a full trial of the case against Alliant and Aerojet. In the view of the Department of Justice, such a trial would involve substantial cost to the United States and is not warranted because

the proposed Final Judgment provides relief that will remedy the violations of the Sherman Act alleged in the United States' Complaint.

VII.

DETERMINATIVE MATERIALS AND DOCUMENTS

A copy of the relevant portions of the contract modification that embodies the negotiated price reduction for the 1992 CEM procurement shall be lodged with the Court to be made available to the public.

No other materials and documents of the type described in Section 2(b) of the Antitrust Procedures and Penalties Act, 15 U.S.C. § 16(b), were used in formulating the proposed Final Judgment.

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Respectfully submitted,

/s/ Howard J. Parker

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