

United States Senate

WASHINGTON, DC 20510

March 18, 2024

The Honorable Lloyd J. Austin III
Secretary of Defense
U.S. Department of Defense
1000 Defense Pentagon
Washington, DC 20301-1000

Dear Secretary Austin:

We write in regards to a recent Government Accountability Office (GAO) report describing the inadequacies of the Department of Defense (DoD or the Department) to track, monitor, and fully understand risks that arise from mergers and acquisitions (M&A) in the defense industry.¹ These findings have important national security implications.

DoD plays an important role in reviewing proposed transactions that may adversely affect competition in the defense industry.² The GAO found, however, that DoD's processes are "not proactive" and do not "analyze the full range of risks that defense-related M&A pose to the defense industrial base."³ These inadequacies can increase supply chain fragility and costs to the Department for products and services provided by an increasingly consolidated defense supply chain.⁴

We included a provision in the *National Defense Authorization Act* for fiscal year 2023 requiring GAO to study the impact of mergers and acquisitions on the defense industrial base and determine whether DoD's current authorities and oversight processes are sufficient to prevent harmful mergers. GAO's report highlights multiple inadequacies of the Department to conduct proper M&A oversight, including DoD's lack of criteria to prioritize M&A that pose the highest risks, insufficient resources to review transactions, lack of data on transactions in the defense space, and failure to monitor the impacts of the vast majority of transactions after they are completed.⁵

The Department of Defense is responsible for assessing actual or proposed mergers that may affect the defense industry. It must evaluate the impact on nine key areas of risk, including

¹ U.S. Government Accountability Office, "Defense Industrial Base: DOD Needs Better Insight into Risks from Mergers and Acquisitions," October 17, 2023, <https://www.gao.gov/products/gao-24-106129>.

² Competition Policy International, "The Department of Defense's Role in Merger Review," David Higbee, Djordje Petkoski, Ben Gris, and Mark Weiss, April 2019, p. 2, https://www.competitionpolicyinternational.com/wp-content/uploads/2019/04/CPI-Higbee_Petkoski_Gris_Weiss-.pdf.

³ U.S. Government Accountability Office, "Defense Industrial Base: DOD Needs Better Insight into Risks from Mergers and Acquisitions," October 17, 2023, p. 33, <https://www.gao.gov/products/gao-24-106129>.

⁴ Congressional Research Service, "The U.S. Defense Industrial Base: Background and Issues for Congress," October 12, 2023, p. 32-34, <https://crsreports.congress.gov/product/pdf/R/R47751>.

⁵ U.S. Government Accountability Office, "Defense Industrial Base: DOD Needs Better Insight into Risks from Mergers and Acquisitions," October 17, 2023, <https://www.gao.gov/products/gao-24-106129>.

national security, innovation, and competition impacts.⁶ DoD also collaborates with the Federal Trade Commission (FTC) and Department of Justice (DOJ) regarding competition concerns,⁷ while also protecting DoD and the interests of DoD stakeholders – including organizations across DoD such as military departments, combatant commands, defense agencies, and DoD Field Activities.⁸ The Office of the Assistant Secretary of Defense for Industrial Base Policy (IBP) has broad authority to identify and determine the need to assess transactions, and the merger and acquisition team has the ability to evaluate these transactions based on their impact on national security, the industrial and technological base, and innovation; the effect on competition for DoD contracts and subcontracts; potential restriction of a critical supplier to a competitor; potential benefits and risks for DoD (including cost savings or increases); and the impact on competition in current or future DoD programs.⁹

The GAO report, however, reveals that DoD policy “does not provide clear direction” and “does not currently have additional guidance to supplement its M&A policy and provide implementation instructions” for which transactions to prioritize when reviewing mergers and acquisitions.¹⁰ As a result, DoD primarily focuses on high-dollar-value transactions that antitrust agencies notify the Department about as a “proxy for identifying which [transactions] present the highest risk.”¹¹ Consequently, DoD “stopped scanning” for smaller transactions, and “infrequently identifies M&A that may present a risk ... outside of antitrust agencies’ request” such as those referred by stakeholders, or those that could be identified as risky by IBP-led trend-analyses.¹²

⁶ U.S. Government Accountability Office, “Defense Industrial Base: DOD Needs Better Insight into Risks from Mergers and Acquisitions,” October 17, 2023, p. 22, <https://www.gao.gov/assets/d24106129.pdf>.⁷ U.S. Department of Defense, Industrial Base Policy, Industrial Base Resilience, Mergers & Acquisitions, <https://www.businessdefense.gov/ibr/gies/ma/index.html>; U.S. Department of Defense, Directive 5000.62, “Review of Mergers, Acquisitions, Joint Ventures, Investments, and Strategic Alliances of Major Defense Suppliers on National Security and Public Interest,” February 27, 2017, p. 4, Section 1.2.b.2., <https://www.esd.whs.mil/Portals/54/Documents/DD/issuances/dodd/500062p.pdf>.

⁷ U.S. Department of Defense, Industrial Base Policy, Industrial Base Resilience, Mergers & Acquisitions, <https://www.businessdefense.gov/ibr/gies/ma/index.html>; U.S. Department of Defense, Directive 5000.62, “Review of Mergers, Acquisitions, Joint Ventures, Investments, and Strategic Alliances of Major Defense Suppliers on National Security and Public Interest,” February 27, 2017, p. 4, Section 1.2.b.2., <https://www.esd.whs.mil/Portals/54/Documents/DD/issuances/dodd/500062p.pdf>.

⁸ U.S. Department of Defense, Industrial Base Policy, Industrial Base Resilience, Mergers & Acquisitions, <https://www.businessdefense.gov/ibr/gies/ma/index.html>; U.S. Department of Defense, Directive 5000.62, “Review of Mergers, Acquisitions, Joint Ventures, Investments, and Strategic Alliances of Major Defense Suppliers on National Security and Public Interest,” February 27, 2017, p. 3, Section 1.1., <https://www.esd.whs.mil/Portals/54/Documents/DD/issuances/dodd/500062p.pdf>; U.S. Government Accountability Office, “Defense Industrial Base: DOD Needs Better Insight into Risks from Mergers and Acquisitions,” October 17, 2023, p. 9, <https://www.gao.gov/assets/d24106129.pdf>.

⁹ U.S. Government Accountability Office, “Defense Industrial Base: DOD Needs Better Insight into Risks from Mergers and Acquisitions,” October 17, 2023, p. 24, <https://www.gao.gov/products/gao-24-106129>. U.S. Department of Defense, Directive 5000.62, “Review of Mergers, Acquisitions, Joint Ventures, Investments, and Strategic Alliances of Major Defense Suppliers on National Security and Public Interest,” February 27, 2017, p. 3, Section 1.2.a., <https://www.esd.whs.mil/Portals/54/Documents/DD/issuances/dodd/500062p.pdf>.

¹⁰ U.S. Government Accountability Office, “Defense Industrial Base: DOD Needs Better Insight into Risks from Mergers and Acquisitions,” October 17, 2023, pp. 16-17, <https://www.gao.gov/assets/d24106129.pdf>.

¹¹ *Id.*, pp. 15-17.

¹² *Id.*, p. 15.

By focusing on high-value, antitrust-agency-requested M&A, DoD is “not comprehensively assessing the M&A of smaller suppliers,” including those that are significant in other ways,¹³ such as those involving companies that “supply critical products to DoD,” produce a “unique military item,” or are sole source providers.¹⁴ This means DoD may overlook mergers that may affect DoD’s capability and capacity to support its mission, result in higher costs to taxpayers, and raise barriers for companies that could otherwise become new vendors.¹⁵ As noted above, DoD policy requires the agency to evaluate nine effects of mergers and acquisitions, including impacts on national security, innovation, and access to critical suppliers.¹⁶ But in each of the cases GAO studied, the only effect DoD evaluated consistently was competition risk. For example, national security effects were not assessed at all as a specific risk.¹⁷ IBP considered competition risks “the only type of risk the antitrust agencies review and can take enforcement action to address,” and is typically unwilling to review non-competition-related risks independent of the antitrust agencies.¹⁸

U.S. antitrust agencies rely on DoD’s input in their review of mergers in the defense space,¹⁹ because the Department is often “the only customer for products and services offered by defense companies.”²⁰ But when FTC or DOJ request DoD assistance, the Department generally only has two weeks or less to provide input.²¹ This short review period is exacerbated by the shortage of staff to conduct M&A reviews.²² As a result, the Department cannot fully assess risks in the initial stages of antitrust review.²³

The primary recommendation of DoD’s own report to address consolidation was “heightened review of any further mergers and acquisitions.”²⁴ DoD has a responsibility to track, monitor,

¹³ *Id.*, p. 17.

¹⁴ *Id.*, pp. 17-18.

¹⁵ Department of Defense Office of the Under Secretary of Defense for Acquisition and Sustainment, “State of Competition within the Defense Industrial Base,” February 2022, p. 1, <https://media.defense.gov/2022/Feb/15/2002939087/-1/-1/1/STATE-OF-COMPETITION-WITHIN-THE-DEFENSE-INDUSTRIAL-BASE.PDF>.¹⁶ U.S. Government Accountability Office, “Defense Industrial Base: DOD Needs Better Insight into Risks from Mergers and Acquisitions,” October 17, 2023, p. 22, <https://www.gao.gov/assets/d24106129.pdf>.

¹⁶ U.S. Government Accountability Office, “Defense Industrial Base: DOD Needs Better Insight into Risks from Mergers and Acquisitions,” October 17, 2023, p. 22, <https://www.gao.gov/assets/d24106129.pdf>.

¹⁷ *Id.*

¹⁸ *Id.*, pp. 22-23.

¹⁹ FTC and DOJ, “Joint Statement of the Department of Justice and the Federal Trade Commission on Preserving Competition in the Defense Industry,” https://www.ftc.gov/system/files/documents/public_statements/944493/160412doj-ftc-defense-statement.pdf.

²⁰ U.S. Government Accountability Office, “Defense Industrial Base: DOD Needs Better Insight into Risks from Mergers and Acquisitions,” October 17, 2023, p. 28, <https://www.gao.gov/assets/d24106129.pdf>.

²¹ *Id.*, p. 23.

²² *Id.*, p. 19.

²³ *Id.*, p. 23.²⁴ Department of Defense, *State of Competition within the Defense Industrial Base*, February 2022, <https://media.defense.gov/2022/Feb/15/2002939087/-1/-1/1/STATE-OF-COMPETITION-WITHIN-THE-DEFENSE-INDUSTRIAL-BASE.PDF>.²⁵ Department of Defense Office of the Under Secretary of Defense for Acquisition and Sustainment, “State of Competition within the Defense Industrial Base,” February 2022,

²⁴ Department of Defense, *State of Competition within the Defense Industrial Base*, February 2022, <https://media.defense.gov/2022/Feb/15/2002939087/-1/-1/1/STATE-OF-COMPETITION-WITHIN-THE-DEFENSE-INDUSTRIAL-BASE.PDF>.²⁵ Department of Defense Office of the Under Secretary of Defense for Acquisition and Sustainment, “State of Competition within the Defense Industrial Base,” February 2022,

and assess mergers and acquisitions with a focus on competition and several other important risk factors. In order to proactively protect taxpayers and national security, DoD should 1) update its M&A policy to specify which transactions require review; 2) shift existing resources to increase M&A review staffing levels; 3) proactively track and monitor transactions, including macro-level trends in the defense industry; and 4) consistently engage in post-merger analysis.

In light of this report, our ongoing concerns with consolidation in the defense industry, and DoD's own concerns with consolidation,²⁵ we urge the Department to adequately resource its merger and acquisition office, conduct holistic analyses on risks to the defense industrial base, and provide information on how the agency intends to do so.

The Department issued its first National Defense Industrial Strategy in January 2024.²⁶ This strategy aims to create “a more robust, resilient, and dynamic modernized defense industrial ecosystem”²⁷ with key areas to include “resilient supply chains,” “workforce readiness,” and “flexible acquisition.”²⁸ It also includes metrics to measure success.²⁹ Given DoD's state of competition report and related deficiencies in the Department's merger review process, this new strategy should also address DoD's plan to address industry consolidation, including monitoring the impacts of mergers and acquisition, as a factor in the health of the industrial base.

Questions

To address our questions about this matter, we ask that you provide answers to the following questions:

1. IBP officials shared with the GAO that DoD programs are able to increase competition by “breaking up a large contract or requirement.”³⁰
 - a. What is DoD's strategy for doing so?
 - b. Is DoD actively doing this with any contracts or programs?
 - c. If so, how often is this occurring? Please provide recent examples.
2. The Defense Production Act³¹ allows the President of the United States and subsequently DoD to influence domestic industry in the interest of national defense. DoD can utilize funding under this authority to “establish, expand, maintain, or restore” domestic capacity

²⁵ Department of Defense Office of the Under Secretary of Defense for Acquisition and Sustainment, “State of Competition within the Defense Industrial Base,” February 2022,

²⁶ Department of Defense, “DOD Releases First-Ever National Defense Industrial Strategy,” January 11, 2024, <https://www.defense.gov/News/Releases/Release/Article/3643326/dod-releases-first-ever-national-defense-industrial-strategy/>.

²⁷ Assistant Secretary of Defense for Industrial Base Policy, “The National Defense Industrial Strategy,” <https://www.businessdefense.gov/NDIS.html>.

²⁸ *Id.*

²⁹ Department of Defense, “National Defense Industrial Strategy,” November 16, 2023, pp. 23-4, 31, 40, 48, <https://www.businessdefense.gov/docs/ndis/2023-NDIS.pdf>.

³⁰ U.S. Government Accountability Office, “Defense Industrial Base: DOD Needs Better Insight into Risks from Mergers and Acquisitions,” October 17, 2023, pp. 11-12, <https://www.gao.gov/assets/d24106129.pdf>.

³¹ 50 U.S.C. § 4501.

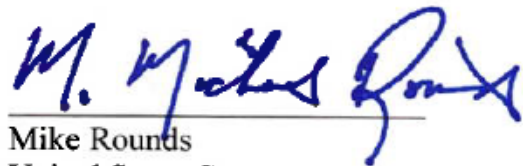
for critical components and technologies.³² What is DoD's plan to improve competition in the defense industry under this authority?

3. IBP within DoD solicits input from stakeholders when assessing mergers and acquisitions.³³ What stakeholders provide this input and how are they chosen? Please provide a copy of any questionnaire or other method used in gathering information from stakeholders.
4. According to the GAO, DoD's M&A team consists of only two to three full-time equivalent employees, which speaks to the Department's failure to prioritize such work. Given the significant and long-standing gaps in M&A review capabilities identified by the GAO report, what has DoD done to address staffing needs to implement merger and acquisition policies, including directive 5000.62, which requires that DoD consider a broad range of potential risks and mergers?³⁴

Sincerely,



Elizabeth Warren
United States Senator



Mike Rounds
United States Senator

CC:

William A. LaPlante, Under Secretary of Defense for Acquisition and Sustainment, U.S. Department of Defense

Laura Taylor-Kale, Assistant Secretary of Defense for Industrial Base Policy, U.S. Department of Defense

³² U.S. Government Accountability Office, "Defense Industrial Base: DOD Needs Better Insight into Risks from Mergers and Acquisitions," October 17, 2023, p. 12, <https://www.gao.gov/assets/d24106129.pdf>.

³³ *Id.*, p. 24.

³⁴ *Id.*, p. 19-21.