Ramparts
30 Nov 1967

Big Brother as a Holding Company

"The contract state of the postwar world must be viewed as a drastic innovation full of unfamiliar portents....Instead of fighting 'creeping socialism,' private industry on an enormous scale has become the agent of a fundamentally new economic system which at once resembles traditional private enterprise and the corporate state of fascism." —H. L. NIEBURG, *In the Name of Science*

[IT'S A SIGN OF THE TIMES]

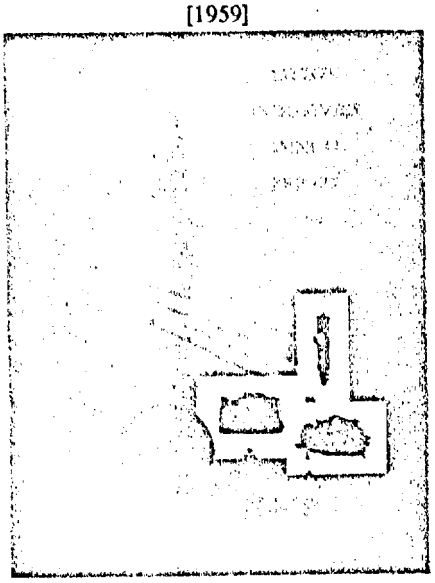
"ACCORDING TO OUR COMPUTER," SAYS Robert Allan Jr., head of Litton Industries' Greek project, "there's less than 800 weeks before the present trend will be irreversible. . . . The need for food and the lack of capacity of technology in . . . underdeveloped nations will be overwhelming. . . . It's time that we got to work on it." To listen to Litton executives and to read their annual reports, one might suppose that Litton was some enormous social welfare agency rather than a multibillion-dollar defense contractor. In reality, it is both of these and more.

Litton Industries produces S&H Green Stamps and Stouffer Foods, missile guidance systems and nuclear attack submarines. It runs important programs of the War on Poverty at home. And abroad it recently secured an $800 million contract—to which Mr. Allan's statement referred—with the Greek military junta for the economic development of the whole geographical region of Western Peloponnesus and Crete. Litton is the perfect example of the new corporation extending itself beyond the limits that have divided the private oligarchies of business from the realms of responsibility traditionally reserved to government.

Already a new crop of names has appeared to describe this development, among them "New Industrial State" and "Contract State," as well as the older and more restricted term, "Military-Industrial Complex." The shape of the new social and economic system that is emerging from behind these labels is as distant from the classical image of "free enterprise" capitalism as is Allan's statement from anything that one might expect to hear from a Calvin Coolidge, much less a Henry Ford.

by David Horowitz and Peter Reese Erlich

[1959]



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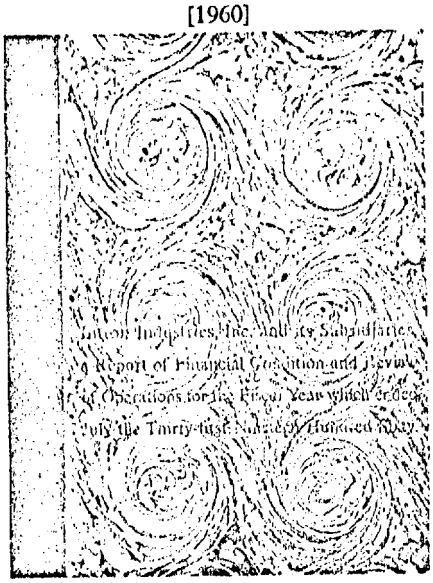

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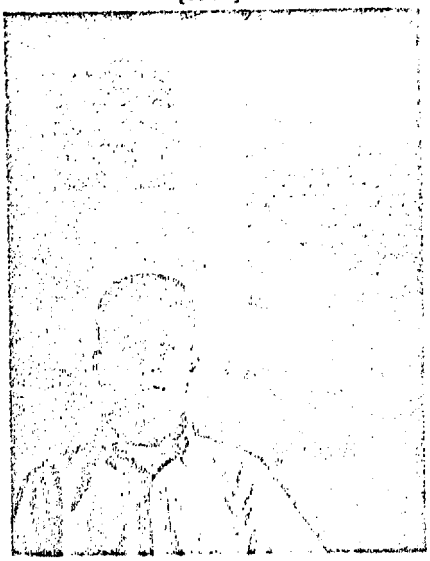


Among the corporate bearers of this brave new American future, Litton stands out as something of a paradigm and archetype foreshadowing the shape of things to come. It is not just the new corporation, but the Now Corporation. It has gathered about itself the full mystique of modernity: advanced technology, the "systems engineering" approach (a product of military contracting), electronics and space. And the mystique has paid off phenomenally well, with a corporate growth rate which Business Week says may well be the fastest in the history of U.S. business.

In 1953, when a group headed by Charles "Tex" Thornton bought Litton, then a small electronics firm, for $1.5 million, the company showed $3 million in sales. This year its worth has grown to a fantastic $1.8 *billion* level, making it the 44th largest industrial corporation in the U.S., ranking ahead of such traditional giants as Alcoa Aluminum, Coca-Cola and Dow Chemical. The aura of futuristic competence that surrounds and powers Litton's conglomerate explosion is reinforced by the higher circles of the business world: Fortune, the Social Register of the business establishment, describes Litton as "the very symbol of all that is modern in U.S. management" and calls its guiding captains "as brilliant a group as can be found at the head of any corporation in the world."

It is perhaps natural that the guiding forces of American society, frustrated by the nation's stubborn social ills which appear to be insoluble by traditional means, should turn to the methodology of military-space development as the Way to Get Things Done. Unable to confront the real moral and political dimensions of its economic and social crisis, the American leadership defines the crisis as basically a technical problem and is immensely comforted thereby: the technical problem is large, to be sure, but it is one that can be handled without any serious reassessment of American values and institutions—and without the social upheaval that might be necessary to restructure them. If engineers employed by private corporations on contract to the government can put men on the moon, it is reasoned, surely they can cure the social and economic crisis at home.

The social engineering approach to race and poverty is merely the logical extension of the pervasive liberal doctrine of pragmatic America and the "end of ideology." As John F. Kennedy, whom many look on as the last national statesman to bear the torch of idealism, affirmed in his famous Yale address in 1962: "What is at stake is not some grand warfare of rival ideologies which will sweep the country with passion, but the practical management of a modern economy. What we need is . . . more basic discussion of the sophisticated and technical issues involved in keeping a great economic machinery moving ahead."

The domestic upheavals in the years following President Kennedy's address have torn to shreds the mythology of the crisis-free welfare state. But the mythology of salvation through the application of technology by the Great Partnership between government and the private corporations has not only survived, it has risen to a new intensity of apocalyptic promise. The theme recurs across the political spectrum, though Democrats may call it a domestic Marshall Plan while Republicans and Wallacites more candidly emphasize Incentives to Business. And if the extension of the contract state means further entrance of a military-social-industrial complex into governance of American society, maybe it is just the right outfit for the job.

LITTON INDUSTRIES WAS THE FIRST corporation to take over one of the poverty program's multimillion-dollar job corps camps—whose large urban centers are now run completely by private enterprise—and was an early promoter of the "military systems" approach for other areas of national policy. As the idea has caught on, proposals have proliferated. General Bernard Adolph Schriever, special Administration consultant on housing and urban development programs, has already suggested that aerospace's management process be applied to these programs, and aerospace industrial teams have begun pushing for contracts in such areas as urban traffic management and water conservation (California's waste disposal program is in the process of being handed over to Aerojet-General). Litton, for its part, has offered to contract whole local school systems, promising to put them on a sound footing and to run them smoothly and economically—a logical step since it is already a major textbook publisher and runs a college of its own in Michigan. It is a proposal that may well appeal to harried parents and tax-ridden homeowners.

Litton Industries has been *the* corporate success story of the postwar period just because it is the perfect product of the times, custom-made to fit the outlines of the new order. For the same reason, it is a perfect image of the economic developments of this period: the vast expansion of the military budget during the Cold War and the largest corporate merger wave in U.S. history.

While the notion of a military-industrial complex has gained currency in recent years, the *technological* underpinning of the new intimacy between government and business has gone largely unnoticed. Yet fully 70 per cent of all research and development being done in the United States today (about $16 billion worth), is paid for by the federal government, whereas a little more than 20 years ago it supported almost none at all. The significance of this for the civilian economy was spelled out recently by Litton's number two man, Roy Ash, in explaining his company's relation to the military sector. Since "almost all new products have their first application in military uses," said Ash, "we always want at least 25 per cent of our business in defense and space."

Ash's statement and the facts behind it reflect the final collapse of the cornerstone of old-fashioned capitalism. In the old days private corporations would develop technological innovations at their own expense, risking the outlay with a view to being rewarded by future returns from the competitive marketplace. This was the very essence of entrepreneurship. However, technical research has now become extremely expensive, and because of the gentlemanly pace of competition among the monopolistic giants of the American economy, these corporations are no longer forced by fear of rivals to risk such investments. So they have become accustomed to getting the government to pick up the tab before they move. These corporations have grown economically lazy, in part because *they* really *can* live better on the largess of the so-called welfare state. One of the factors that has made it possible for them to pry such huge sums of research money out of the government has been the unprecedented increase in the concentration of economic—and with it, political—power in the last decade.

This tremendous concentration movement in the economy has been spearheaded by the advance of the "conglomerate" corporations, formed by the acquisition of companies operating in diverse markets. Litton is the star of this movement, with enterprises in 18 distinct industrial categories.

To an uninitiated observer of the conglomerate phenomenon, Litton's fantastic rise has a distinctly mystifying air about it, like some kind of psychic levitation. For despite all the hullabaloo about new technologies and go-go management, Litton can point to no revolutionary innovation which has benefited the civilian economy and represents a tangible basis for its surging nonmilitary growth (about two-thirds of Litton's present sales, according to Roy Ash, are in civilian fields). One has only to think of Xerox and Polaroid, where jet-powered corporate growth and revolutionizing technology have gone hand in hand, to bring the contrast into focus. It is not that Litton produces nothing innovative or useful (if inertial guidance systems for missiles and fighter planes can be considered useful), but rather that nothing Litton has marketed seems to warrant its unparalleled record of corporate expansion. Indeed, most of Litton's technological innovations were already being developed in the 70 and more businesses which Litton has acquired—***before*** they became part of the parent firm.

Yet to be mystified by this is merely to confuse what Thorstein Veblen called the "business system" with the industrial system—that is, to mistake the system of developing and implementing technologies to meet human needs for the system of making a buck off them. Litton's success is a function almost entirely of a brilliant, if sleight of hand, business strategy, with the U.S. government as silent partner. If the constituents of its success seem somewhat insubstantial to the ordinary man, the cash it has made is real. And in the "business system," it is the cash that counts.

To mastermind such a success in the business world, as in the theater, one must learn to live in an attenuated universe where the fictitious is more tangible than the real. At a very early age, Tex Thornton, the brains behind Litton, learned just that.

[GROWING UP WITH TEX]

"Tex Thornton—good abilities along a few lines but not a good all round man; is unprincipled, ruthless and is universally disliked; cannot be trusted."

—FROM A CONFIDENTIAL MEMO PREPARED BY A MEMBER OF THE PRESTIGIOUS WALL STREET ACCOUNTING FIRM OF HASKINS & SELLS; MARKED AS AN EXHIBIT IN THE STEELE VS. LITTON CASE.

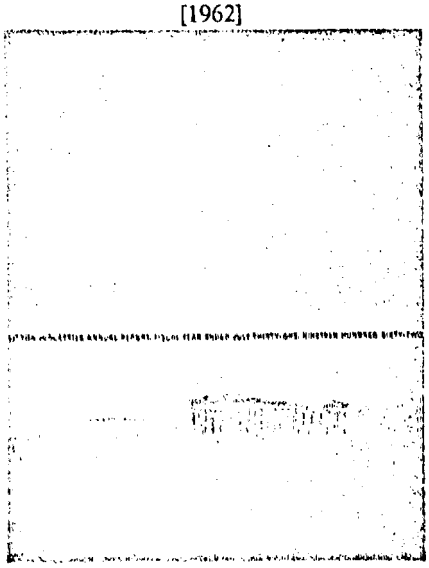
TEX THORNTON IS THE PARADIGM new corporate manager of the paradigm new corporation. His career follows the now well trodden path from civilian Washington to the military to the corporate elite.

Thirty years ago Tex Thornton was a $1400-a-year clerk in Washington; today he is a university trustee, a member of the President's Advisory Commission on Civil Disorders (the Kerner Commission) and head of its special Advisory Panel on Private Enterprise. He was one of a handful of nominees considered to succeed Robert McNamara as secretary of Defense, and according to a Washington Post columnist he is—with typical military-industrial bipartisanship—presently being considered by Richard Nixon for that job. He has already achieved the coveted seat next to the President at White House business meetings. In addition to being chairman of the board of Litton, he is an "interlocking director" of such giants as TWA, Lehman Corporation, General Mills, the Western Bancorporation (a bank holding company for the Bank of America interests) and Union Oil. Needless to say, in Thornton's new circles being a millionaire is not at all unusual, but he has already made $80 million and is aiming for the status of centimillionaire. If the market for Litton stock holds up, he will soon make it. Tex Thornton has come a long way, and the Horatio Alger award he received in 1964 was shrewdly given.

Soon after Tex was born in a small north central Texas town, his father ran off, leaving his mother to drill him in the manly art of finance. When he was just twelve, she was already encouraging him to use his earnings from odd jobs to buy land, instead of frittering his money away like a kid. He eventually accumulated nearly 40 acres. By the time Tex was fourteen, every store in town would accept his personal check. And he was all of nineteen when he launched his first real business venture: a combination gas station and Chrysler-Plymouth dealership.

Later, setting his sights always higher, he enrolled in Texas Technological College, starting first in engineering, but switching quickly to business administration—after all, the engineer

[1962]



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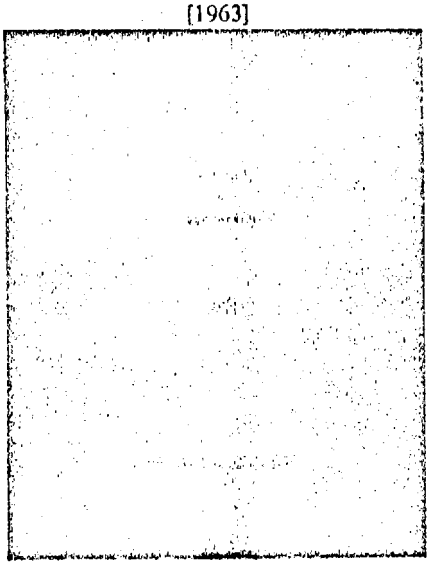

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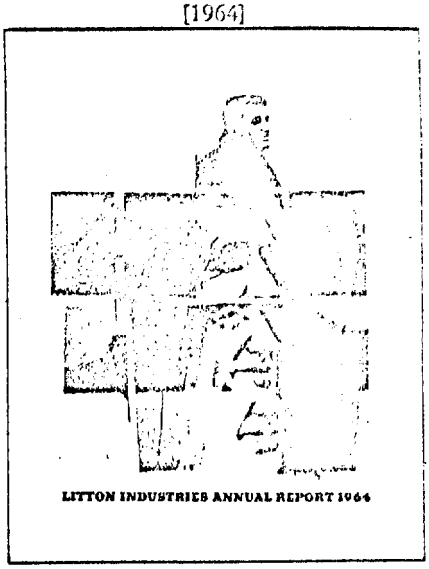


works for the businessman. He quit Texas Tech in his junior year and took off for Washington to check out the action in the School of Life. In Washington he returned to college and got his Bachelor of Commercial Science in 1937. His first job was as a clerk in the Department of the Interior.

For four years Tex was unable to find that combination of business-military-political influence which he needed to power his ascent. When he did find it, its name was Robert Lovett, Wall Street banker and assistant secretary of War. Lovett was not just a run-of-the-mill Wall Street banker, either; he was destined to become—in the euphemism of such a scholar as Arthur Schlesinger Jr.—one of the co-chairmen of the American establishment. Highly impressed with the twenty-eight-year-old Tex, Lovett suggested that he join the Army (it was pre-Pearl Harbor 1941) as a second lieutenant. Apparently a brilliant officer, Thornton received his first promotion within 48 hours. A series of such jet-assisted takeoffs made him one of the youngest full colonels in the U.S. Army, at one point with as many as 2800 *officers* working for him around the world. Like the present secretary of Defense, Clark Clifford, whose military career had a striking resemblance to Thornton's [see RAMPARTS, August 24, 1968], Tex never left his desk. Yet the War Department honored him with a Legion of Merit, a Commendation Ribbon with two oakleaf clusters, along with a Distinguished Service Medal that Tex still wears on his lapel. "It's the kind of thing a guy would wear," observes one of his detractors, "if he wanted you to think he had been a big combat hero during the war."

It was at this point that Tex's instinct for the Combination manifested itself. The federal government, with an assist from banker Lovett, had gathered, as if for Tex's own benefit, an array of managerial talent which, if offered in the right package on the business market, could command a premium price. So Tex organized nine of his subordinates into a team—later known as the Whiz Kids—and offered it to Henry Ford II with price tags of around $10,000 a year each on the nine, and $16,000 on himself, the commanding officer. With Lovett's blessing, Tex sold his package. Ford did not do too badly on the deal, gaining four future divisional bosses and two presidents of the company, including Robert Strange McNamara who was later to become—on Robert Lovett's nomination—secretary of Defense.

AT THIRTY-TWO TEX HAD BECOME director of planning for one of the giants of U.S. industry. Within only a few years, however, Thornton's ambition brought him into collision with his superiors at Ford. So he offered his services to Hughes Aircraft. Apparently, Thornton was not exactly welcomed with open arms. Noah Dietrich, then financial head of the company, strongly objected to hiring him. But with the help of two of Tex's old Army buddies, Generals George and Eaker, who were on the board, Dietrich was overruled. As assistant general manager Tex took command of operations and hired his future right-hand man, Roy Ash—a Bank of America statistician with no accountancy training—to be assistant comptroller. Ash had been one of Thornton's subordinates during the war.

Hughes' business, especially with the newly independent Air Force, boomed. In 1948, Hughes did a total of $2 million in sales. By 1953, when Thornton left Hughes, the figure was $200 million. The biggest boost came from the Korean War and an exclusive contract to produce a special Fire Control System (a device to regulate the firing of aircraft guns). The contract with the government for the control system was on a "fixed price, redeterminable" basis; that is, a price was agreed on at the outset which could be "redetermined" if costs increased. Based on the ongoing costs of material, Hughes received periodic "progress payments."

Thornton and Ash were very anxious to have Hughes Aircraft make a profit on this contract—a little too anxious, it would seem. According to sworn court testimony which convinced the jury in the case of Steele vs. Litton Industries (although the judge suspended the verdict on a legal point), and a number of other suits and counter-suits, the following picture emerges:

Hughes Aircraft's accounting department was unable to keep track of the costs under the fire control contract and began falsifying the affidavits they were required to submit to the government regularly, stating the current costs. Thornton and Ash found out about this, but far from stopping the procedure, they encouraged it. James O. White, one of the company's accountants, gave the following testimony:

Q: In substance, did somebody tell you that Mr. Thornton had said that, "We want to file false affidavits"?

A: In substance, yes.

Q: Who was this?

A: Ash.

Q: What did he say?

A: He said, "Tex wants to get the money and we're to do it any way we can to get it."

Another means of cheating the government was artfully described as "midnight requisitions." Clerical personnel were called in after-hours and on weekends and told to fill out millions of dollars worth of phony requisitions. Again James White's testimony explains:

"They [the requisitions] were filled out by people who had no knowledge of the facts, who had not used the parts, who had not withdrawn them from stores. They were put into the records as though they had. They were made to look as though they had been proper. They were backdated. They were made to look as though they had been handled by factory people instead of office people, dirtied, in other words, to make them look old and genuine as having come through the shop. They were complete forgeries."

Eventually a group of five CPA's revolted and refused to continue these procedures for fear of losing their certificates. When they told Thornton they would resign, he told them to be quiet and be "good company men." They went to General Harold George, nominally head of the company, but his position was that, "This is something . . . generally indulged in by other military contractors," and he "didn't think there was anything out of order."

The CPA's resigned after taking their case to the Hughes directors. But Secretary of the Air Force Harold Talbott had already learned of the indiscreet management at Hughes and had given Howard Hughes himself an ultimatum: "Either change your management or sell the company. By God, I'll give you 90 days."

On September 1, 1953, Howard Hughes locked Thornton and Ash out of their offices. By February of 1954, Hughes Aircraft had paid back some $43 million to the Air Force which had been "misappropriated" during the stay of Thornton and Ash.

THE LOCKOUT AT HUGHES WAS TEX Thornton's lucky day. For at the same time as he was being kicked out, there was a massive walkout of disgruntled top engineers and executives, men who went on to found such stars of the conglomerate aerospace field as TRW and Teledyne. Tex managed not only to lose himself in the exiting crowd but also to take some talent with him. Emmett Steele, with an ingratiating personality and invaluable contacts in the Pentagon, was to become his sales manager, and Hugh Jamieson his top engineer.

Meanwhile, Charles V. Litton, owner of Litton Industries, having suffered a family tragedy, was ready to sell his small electronics firm. And Thornton and his team were on the lookout for just such a deal. However, Litton apparently regarded Thornton as untrustworthy and was reluctant to sell to him. At one point he even broke off negotiations. According to Litton, it was Jamieson and Steele who finally convinced him to sell. (This was a key point in the breach of promise suits which the two later brought against Tex for allegedly defrauding them of their original shares of founders' stock. Jamieson, who had agreed to testify in Steele's case as well, suddenly settled out of court for a sum estimated at anywhere from $3 million to $20 million.)

With Litton ready to sell, all that Tex needed was cash to consummate the deal, and that meant a trip back to Robert Lovett's milieu and the giant investment banking house of Lehman. Joe Thomas, Lehman's partner and a fellow Texan, provided $1.5 million to buy Litton, in exchange for 75,000 of the original 575,000 shares. Common stock cost Lehman's investors ten cents a share. During the next decade and a half it sold for as much as $150. It was no doubt one of the best deals the Lehmans had cut since they helped finance the slave South's cotton crop during the Civil War.

[NUMBERS GAMES]

". . . it was obviously only a question of time before some smart fellows would start building companies not around the logical progression of a business but around what would beef up the numbers." —"ADAM SMITH," *The Money Game*

WHEN TEX THORNTON AND COMPANY took over Litton, it was essentially a laboratory production office, a very modest enterprise. After four years under the new management, Litton's annual sales had risen from $3 million to $100 million—and that was just the beginning.

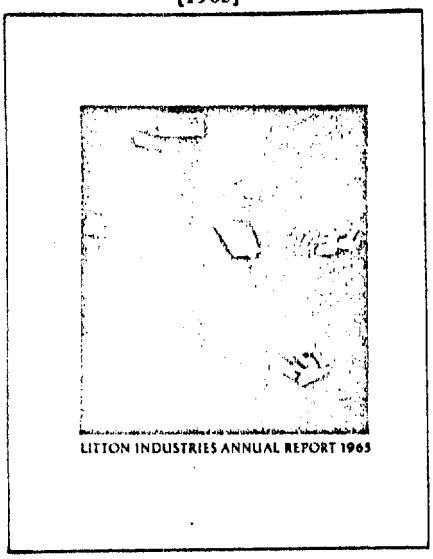
The traditional conception of the growth of a business brings to mind images of the firm selling more of its products, creating new ones, and building new plants to produce more to sell. Only a fraction of Litton's growth, in fact, was achieved in this way. Of the $97 million increase during Tex's first four years, for example, sales from Charlie Litton's original firm accounted for only $11 million. The rest of the increase in sales resulted from the acquisition of some 17 previously existing companies and their incorporation into a new overall financial superstructure: "Litton Industries, Inc." As Thornton explains, "We had to grow fast. There wasn't time to learn a business, train people, develop markets. . . .We bought time, a market, a product line, plant, research team, sales force. It would have taken years to duplicate this from scratch."

Buying, not building, was the formula of Litton's growth. To understand how a small firm with limited resources *can* buy itself into bigness, one must understand how corporate growth can feed on itself. For the very act of merger creates new power to merge on an even larger scale through its effect on the value of the corporation's stock.

The value of the stock and therefore of the corporation is not determined by adding up the values of tangible assets: cash reserves, inventories, equipment, plant and so forth. The value of the stock is determined by what people are willing to pay for it, and they will pay more now if they expect its value to rise in the future. Of course these are not just expectations of expectations, but are ultimately derived from an assessment of the potential for real growth of corporate assets and earnings.

Expectations, however, are by nature intuitive, and intuition can be influenced by all kinds of intangible factors. Jack Dreyfus, head of one of the biggest mutual funds on Wall Street, once commented wryly on the subjective "glamour" factors which have gone into making the stock of corporations like Litton highly valued on the market, by offering his own prescription for such a success: "Take a nice little company that's been making shoelaces for 40 years and sells at a respectable six-times-earnings ratio. Change the name from

[1965]



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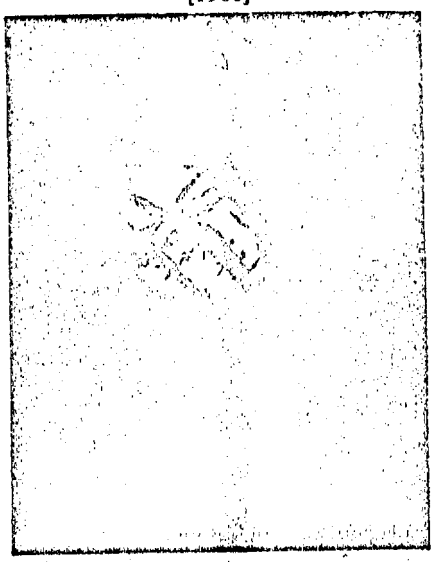

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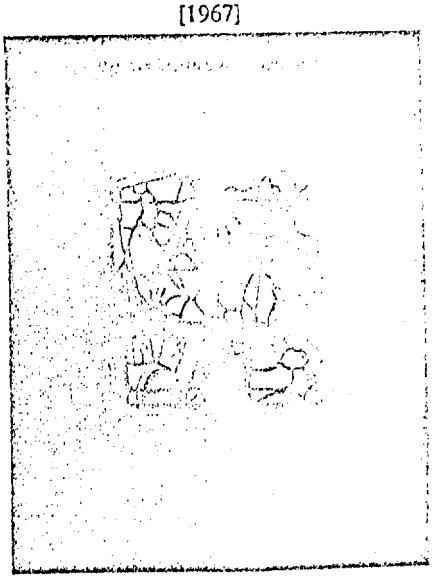

Shoelaces Inc. to Electronics and Silicon Furth-Burners. In today's market, the words 'electronics' and 'silicon' are worth 15 times earnings. However, the real play comes from the word 'furth-burners,' which no one understands. A word that no one understands entitles you to double your entire score. Therefore, we have six times earnings for the shoelace business and 15 times earnings for electronics and silicon, or a total of 21 times earnings. Multiply this by two for furth-burners and we now have a score of 42 times earnings for the new company."

The key to conglomerate growth is the fact that a company's stock can be—and ordinarily is—the "money" that is used to purchase another corporation. So a smart businessman can make the process come full circle. By successfully creating a glamorous "growth image" on the stock market that excites expectations of real future growth, he can drive the value of his stock up. This then gives him new "money" with which to buy *real* assets in the form of another corporation: in other words, his business can grow in fact and not just on paper, thereby confirming the expectations he aroused and further strengthening the image. And so the circle becomes a spiral of increasing growth.

It is small wonder, then, that creating a glamour image is a major preoccupation of conglomerate managements like Litton's. Indeed, Litton was a pioneer in converting the traditionally staid Annual Report to Stockholders into a high-class Advertisement for Myself. Litton's reports look more like catalogues from Pasadena's Huntington Museum of Art than informational materials from a major industrial corporation. Abraham J. Briloff described it in the Financial Analysts Journal: "Litton's 1967 report is, as you undoubtedly know, a most beautiful document . . . which symbolizes the ethics of 20th century commercial life in the New Industrial State . . . distorted in my view is the series of graphs most beautifully set to type at page 55 of the annual report. . . . The curves which the eye is invited to make are optical illusions capable of inducing inappropriate investment decisions."

Another art which is employed in the production of a glamour image is creative accounting. This important technique of the Big Growth game is made possible by the looseness of the principles under which firms are audited. The usual methods are not as crude as those that were used at Hughes Aircraft, but their effects can be pretty significant.

As the pseudonymous "Adam Smith" notes in *The Money Game*, "Numbers imply precision, so it's a bit hard to get used to the idea that a company's net profit could vary by 100 per cent depending on which bunch of accountants you call in, especially when the market is going to take that earnings number and create trends, growth rates, and little flashing lights in computers from it. And all this without any kind of skulduggery you could get sent to jail for." An explanation for this legal generosity was given by the real Adam Smith, the 18th century prophet of the free enterprise system. The very purpose of government, he wrote, was "to secure wealth, and to defend the rich from the poor."

THE SPREAD BETWEEN ONE SET of figures and another can be the difference between a real glamour stock and a merely good performer, as evidenced by Litton's 1967 report, which with one flick of the accounting wrist boosted the figure for the increase in the corporation's earnings over the previous year from 15 to 26 per cent. This was accomplished by ignoring the pre-merger earnings of newly-acquired companies when estimating the increase. And this is only one of the gambits available to merger oriented firms. As "Adam Smith" observes, "If you are busy buying and selling companies, every time they pass through your accounting firm you get the chance to try to describe artistically some of the assets as earnings, to capitalize costs that have previously been expensed, and in general to create what Wall Street is looking for, which is a neat pattern of constantly growing earnings."

Conglomerates are so obviously based on highly speculative, not to say shady, principles that even the Wall Street Journal has been prompted to take off its gold-rimmed rose-colored glasses for an instant and ask a few probing questions about them: how much of their growth is based on improved products and efficiencies and how much reflects the attractive arithmetic of acquisition and the temptations of empire building? . . . Can they be managed efficiently?

This last question has an especially poignant ring for Litton's supermanagers. In 1968, Litton's second quarter report admitted a disastrous 30 per cent earnings drop (Litton's stock

price plummeted nearly 50 per cent at the news), reflecting managerial errors so gross that not even the most creative accounting techniques could cover them up.

The mistakes affected several of Litton's divisions, including its business furniture, Royfax duplicators, Monroe calculators, and its Royal typewriter line. But the biggest error of all provided the clue to the overall pattern of Litton's debacle. The Litton shipyard, which had been accustomed to a rich diet of cost-plus contracts at the government trough ("Your chances of losing money" under such contracts, admits a Litton executive, "are not too great"), had for the first time bid competitively on a package basis for the construction of automated merchant vessels—a *civilian* contract under which you don't get to come back for more money if you can't make it at the agreed-upon price. The result of this market test was that Litton underestimated the costs, submitted a bid that was too low, and instead of netting a profit, had to write off a loss of $8 million.

In what must rank as the understatement of the year, Fortune, after noting that the key to Litton's setback was its inability to stand the test of the relatively competitive civilian market, observed: "The requirements for profitability in government work are less exacting than those of the private marketplace." They certainly are.

Under government contracts there is a decided lack of competitive strictures. Little or no capital is risked by the corporation. If it makes errors of judgment, timing, cost analysis and so forth, there are no competitors to take advantage of its mistakes. And it has an enormously understanding buyer. If costs are underestimated, they can always be adjusted up through contract renegotiation. One former Litton executive with responsibilities in this area estimated that as a matter of *normal* practice, Litton in the course of production and development renegotiated its contracts to one and a half times the original price—a nice margin for inept planning and mismanagement.

In short, its vulnerable, soap-bubble growth strategy could never have carried Litton so far had it not possessed the ability, though a small firm at the outset, to get a front-line position in the prime military contract game and latch on to that secret fuel which alone can launch space age corporations towards the moon: the financial largess of the state.

[CONTRACTING NATIONAL SECURITY]

. . . the creation of the U.S. Air Force as a separate military service . . . may have had more important consequences for U.S. industry than any other event in recent decades."

—FORTUNE, SEPTEMBER 1968

THE HIGH POINT OF LITTON'S close connections in Washington was reached during the reign of Tex Thornton's one time subordinate, Robert McNamara, as secretary of Defense. Thornton, who was often a breakfast guest at the Pentagon, claims never to have talked business with the secretary during those visits. But, as the executive of another corporation in the contract field observed in a RAMPARTS interview, "A clever man would merely let it be known that he was having breakfast with McNamara every other morning. When talking to procurement officers and the like, he wouldn't even have to mention McNamara's name."

The subtle but far-reaching significance of good connections was pointed out by the leading student of the military-industrial complex, Professor H. L. Nieburg: "Officials in the lower reaches of the government bureaucracy (both civilian and military) charged with administration of contracts, find themselves dealing with private corporate officials who often were their own former bosses and continue as companions of present bosses and congressional leaders who watchdog the agencies. A contract negotiator or supervisor must deal with men who can determine his career prospects; through contacts, these industrial contractors may cause him to be passed over or transferred to a minor position in some remote bureaucratic corner, sometimes with a ceremonial drumming before a congressional committee."

Among Litton's vice presidents are Joseph Intirie, a former undersecretary of the Air Force, and John H. Rubel, a former assistant secretary of Defense (a key member of the McNamara team). But what may be Litton's most important connection is Tex's close friendship with George Mahon, chairman of the vital House Appropriations Committee. Mahon's Texas district lies near Thornton's home town, and Tex has been friendly with him since the Whiz Kid days at Ford. According to the previously quoted executive, Mahon "is a very dedicated public servant, but he doesn't know how to handle the power he has. This friendship [between Mahon and Thornton] has had more to do with the growth of Litton's military contracts than any other factor. Tex has played Mahon like a fiddle."

But political strings are only half the story. More than anything else, it is the defense contracting system itself, as it evolved after World War II, which has created the new and sinister relationship between the giant corporations and the state.

Following the profiteering scandals of World War I, which revealed that American business had milked the American taxpayer by "sliding" price policies on military contracts, and had spent the lives of many American soldiers by producing cheap, shoddy equipment, the practice of competitive bidding on government contracts was instituted to simulate the open market. The two armed services developed their own "in-house" design and production capabilities which served to measure and check outside performances. Under the pressures of the Second World War, contracting procedures on aircraft, ordnance and ammunition reverted to the cost-plus basis which had inspired the earlier scandals. Then a series of developments after the war produced the current unprecedented state of affairs.

First, as part of a movement heralded as a return to "free enterprise," plants, factories and facilities built by the government during the war were either sold to private corporations, usually at a fraction of their original cost, or were leased at nominal fees to contractors, to use for military contracts. This largely deprived the government of the performance "yardstick" of its in-house facilities.

Second, the Air Force was established as an independent military service. Naturally, it did not have the already built in-house capabilities of the other two services, so it hired out the entire process of designing, producing and even maintaining weapons systems, instead of presenting its own designs to contractors for production. This necessitated a cost-plus contractual basis, since no prearranged price could

be fixed for so indeterminate a process. In addition, the Air Force's prime contracting corporations, now responsible for complete weapons systems, had to establish, in the words of one Congressional Report, "procurement organizations and methods which proximate those of the government." These prime contractors were thus in a position to force subcontracting small companies out of business, acquire their proprietary information, make or break geographical regions and decide a host of other critical issues of national import, without even the quasi-democratic checks imposed on the federal bureaucracy. No wonder H. L. Nieburg has warned of the ominous erosion of public control by the giant aerospace companies and has dubbed the whole relationship "the contract state."

Once established, prime systems contracting quickly spread to the other services. A losing battle with the Air Force for responsibility for missile program development taught the Army that its extensive in-house capabilities and technical independence were a distinct disadvantage. For in the political struggle over missile development, the Air Force's corporate prime contractors constituted a powerful lobby in Congress against which all the in-house expertise of the Army was of no avail. A quick learner when the future of its bureaucracy is at stake, the Army began to disband its in-house facilities and to surrender its jurisdictional and discretionary capacities to private industry and the latter's impressive political power. For any corporation in advanced technologies on the way up, prime contracting soon became the indispensable order of the day.

FROM THE OUTSET, THE NEW Tex Thornton team at Litton had its eyes on the really big electronic equipment and systems markets. They were determined not to be pikers and they knew their way up the federal escalator, but they needed a break. In 1954, a team of Litton scientists headed by Dr. Henry Singleton appeared ready to give them one. He outlined a project for miniaturizing an inertial navigator and guidance system. Perfecting such a system was of paramount importance to the military, for it would be the only kind of navigational system that could not be electronically jammed. Further, a missile guided by such a navigator would not emit signals that would disclose its whereabouts. The military had already set out the objectives of such a system and various working devices had been produced, but they all weighed from 500 to 1000 pounds, too heavy for aircraft and missiles. Thus, Singleton was proposing an innovation that would revolutionize the field.

All that was needed to attempt to develop the system was capital. Of course the Litton management, well oriented towards the new age, had no intention of putting up their own money, or of raising it through old-fashioned loans or investors. For to raise capital in that way would entail risks and obligations. What Litton really needed was a banker who would not seek repayment of capital (with interest) if the investment bore no fruit, and if the project should come through, who would not insist on reaping any return on his investment. Could there *be* such a banker? Litton thought so.

With nothing but a wooden mock-up of the proposed navigator and a ten-cents-a-mile expense account for its station wagon, the Litton sales team set out to sell a miniaturized inertial navigation system to the Army Air Corps. In 1956, they finally convinced the purchasing agents at Fort Huachuca, Arizona, to finance the development of a prototype. For its proposal, Litton got a fixed price redeterminable contract for $214,902.

With the Fort Huachuca contract safely tucked away in their display kits, Litton salesmen then made the rounds of various other government agencies and aerospace firms, stressing the advantages of getting in on the ground floor with contracts for the navigators while the opportunity lasted. In 1957, Litton contracted to produce for Grumman, the chief Navy aircraft supplier, 68 of the navigators for Navy planes. By 1959, this contract was worth some $7,400,000. In subsequent months, Litton used its new foot in the door with Grumman to sell them additional items, until their total contracts amounted to a full $10 million.

According to the Steele case testimony of John McDonald, then head of Litton's electronics division's contract negotiations, Litton's engineers did successfully achieve the new revolutionary design. But Litton never delivered the prototype navigator to the Army, which had originally paid for it; instead, it used the design to fulfill its contract with Grumman Aircraft. All the Army got was a bagful of disassembled parts. In 1960, the Army purchasing officials canceled Litton's contract "for the convenience of the government."

As for Litton, it had won for itself a tremendous future contracting position for electronics and guidance systems in missiles, planes and even ships, on which all the federal giveaways on costs and profits would be multiplied a thousandfold. No longer a little laboratory but a real comer in the field, Litton was now ready for a really golden opportunity: a major subcontract for the guidance system of the F-104 Starfighter jet. And when Germany decided to incorporate 700 F-104's into its postwar *Luftwaffe*, Litton bought two German companies just to produce the guidance systems for their version of the plane. Unfortunately, the *Luftwaffe's* Starfighter turned out to be, in the words of Business Week, "an essentially American product that now bears the blackest name in the history of German aviation." At least 83 of the planes crashed, killing 42 pilots and forcing Litton to modify the guidance system. Some time later a further modified version of Litton's navigator was installed in America's newest fighter plane, the ill-fated F-111, McNamara's notorious pet project and one of the costliest boondoggles of all time. The prime Navy contractor for that plane: Grumman Aircraft.

[CONTRACTING A MODERN INDUSTRY]

"The aerospace industry, with its intimate contacts in the Department of Defense, is making its move now to take over the entire maritime industry in the United States. Unless the maritime industry recognizes its real enemy, the military-industrial power of the aerospace industry will suceed."

—FROM A FULL PAGE AD IN THE NEW YORK TIMES, OCTOBER 24, 1966, PLACED BY THE CHAIRMAN OF THE BOARD OF THE NOW DEFUNCT SAPPHIRE STEAMSHIP LINES.

THE AMERICAN MARITIME INDUSTRY had been ailing badly since World War II. Even the captive business of the U.S. Navy and a big federal subsidy on non-military business (paying the difference, up to 50 per cent, between U.S. shipbuilders' inflated prices and those of foreign rivals) couldn't sustain sales. The Swedes and the Japanese had surpassed them technologically, and protective government assistance had merely allowed the gap to widen. So

in the early 1960's, the U.S. Navy, which bought 80 per cent of the industry's output anyway, decided to act.

The Navy—then the last holdout—decided to adopt the Air Force's "total package" or "weapons system" approach: a single shipyard would be given a supercontract to design a ship and build a fleet of them. The extraordinary scope of the order would require the contractor to build a new shipyard with modern assembly line features unavailable in then current U.S. shipyards. And because the contract was for a total package, the contractor would have to plan everything from the skills of the crew to the maintenance requirements.

Of course no one in the maritime industry at that time was even remotely equipped to handle this kind of operation. In essence, it was a plan to vault over these moribund corporations, arriving in one jump at a new technological level by turning the shipbuilding business over to the only corporations who were already equipped for the "systems" approach: in a word, aerospace. And among the aerospace corporations, those fortunate enough to have had a head start in the maritime field would naturally be ahead of the game.

The Navy did not announce its decision to adopt this new approach until after 1963. But long before the announcement came, Litton somehow managed to get a sniff of what was in the wind. As Roy Ash explained, "We saw some developments coming and thought we could be a part of them. One thing we foresaw was an expansion of the practice—it was already established in the Air Force and for Navy aircraft—of turning to industry for help in developing total weapons systems." So in 1961, Litton picked up Ingalls, an ailing shipyard with $60 million in annual sales, for $8 million and an agreement to pay $9 million in debts to the Navy. Ingalls got a number of contracts over the next few years—for one amphibious assault ship here, six cargo ships there.

Then in November 1965, the big deal went up for grabs: McNamara announced approval of a large integrated system of Fast Deployment Logistics (FDL) ships. These "floating warehouses"—perhaps as many as 30 of them—would be stationed strategically around the world, ready to move quickly into "trouble spots" to back up U.S. troops with ammunition, C-rations, tanks, etc. The FDL was the first ship to be handled under the Navy's new weapons system approach.

Several shipbuilding companies were in the initial bidding for the contracts, but they all either dropped out or were eliminated. The final stage of bidding included three aerospace giants: Litton, General Dynamics and Lockheed. Each got $5 million in contracts to finish plans for the FDL and the yard. Of course each would need a site for its yard. According to the Wall Street Journal, climate ruled out New England and the steep cost of steel and highly unionized labor made the West Coast undesirable. That left the U.S. domestic colony of cheap labor: the South.

Litton, of course, luckily already had a location in the South, in Pascagoula, Mississippi: Ingalls shipyard, to be exact. But they still needed to find a way to finance the new yard, which according to informed sources at the time would cost $100 million to build. And this time the federal government was not putting up the money. But there are state governments too. Already the largest employer in Mississippi, Litton went straight to the state capital and threatened to take their new yard to Tampa, Florida, if they did not get cooperation. Mississippi quickly agreed to build the most modern shipyard in the world and hand it back to Ingalls on lease at a minimal price. Governor Johnson called a special legislative session in order to pass a $130 million bond issue (the extra $30 million was interest). In October 1967, the bond issue was approved by Mississippi voters.

Of course the people of Mississippi would "own" the leased-out shipyard, though they would not reap the profits from or control its operation. For their $130 million investment they would get an estimated 12,000 jobs, at Pascagoula wages and under special "long-term" union contracts ("yellow dog" is such an old-fashioned phrase). Litton also rewarded its Mississippi friends by writing into its contract the latest in sophisticated legal loopholes to help the shipyard bosses keep blacks out of the good jobs for as long as possible.

Yet, despite all this stage setting, Litton still had not been awarded the contract. So they set 200 experts to work on a winning design, under complicated and difficult new CF-CD (Contract Formulation; Contract Definition) procedures that had been worked out by McNamara's assistant secretary of Defense, John H. Rubel.

Once again, Litton was in luck: in the interim Rubel had shuttled over from the Defense Department to head the Litton team working on the bid. Having helped toss the plum in the air, he was right on the spot to catch it. Unfortunately, however, just as Litton won its $2 billion prize, the project hit a snag. Congress refused, first in 1967 and again this year, to appropriate the money for the FDL's. In the Senate debate even Richard Russell, chairman of the Armed Services Committee, expressed concern that the ocean-going bases might contribute to "an impression that the U.S. has assumed the function of policing the world and can be thought to be at least considering intervention in any kind of strife or commotion occurring in any nation of the world." Of course, an embittered Litton backer might note that military land bases may have a special place in Senator Russell's heart, since he has blessed the construction of 19 of them in his home state.

But do not fear for Litton; it is an unwritten law of the contract state that what the Navy brings to birth it does not allow to die. The Navy will see that Litton, its answer to the decrepitude of the U.S. maritime industry, is well taken care of. Since the first congressional slash, the Navy has already salved Litton's wounds with at least $1.2 billion in new contracts.

And Litton's now modernized shipbuilding enterprise, which has already become the largest producer of automated cargo ships in the world, can still, like the older maritime companies, mark up its price to civilian buyers 50 per cent above the prevailing world market price and have the difference paid by U.S. taxpayers—through the nose. Litton's relationship with the Navy was summed up quite well by Senator Stuart Symington: ". . . Litton has got the whole bag now."

Part Two of this article, appearing in the next issue, describes the most recent—and far-reaching—developments in the odyssey of Litton Industries and the contract state, the further supplanting of the political process in the governance of American society. Chapters in this episode include the disturbing stories of Contracting International Development (in fascist Greece) and Contracting Poverty ("welfare" and the education of the poor).

Researchers on this story: Jan Austin, Lee Webb, Peter Wiley.