Huntington Ingalls Industries

August 03, 2012

U.S. Department of Commerce
Hillary Hess
Office of Nonproliferation and Treaty Compliance
14th Street and Pennsylvania Avenue, NW
Washington, DC 20230

Subject: RIN 0694-AF65 Rule Comments

Dear Ms. Hess:

Huntington Ingalls Industries (HII) welcomes the opportunity to provide the following inputs to the Federal Register Notice of Proposed Rule, dated June 21, 2012, regarding the Implementation of Export Control Reform.

I. Specialized Treatment of "600 series" Products and Technologies

The proposed rule provides explanations for many aspects of the transition; however, it includes changes to the Export Administration Regulations (EAR) not previously anticipated. The most unexpected difference revolves around the special treatment of "600 series" products and technologies separate and distinct from other items "subject to the EAR". If interpreted correctly, the transition to the EAR from the International Traffic in Arms Regulations (ITAR) would yield, in essence, the creation of a third controlling regime for the processing of "600 series" export shipments. The burden associated with applying the specialized "600 series" requirements in everyday international business is expected to be time consuming, confusing, and costly. It is HII's recommendation that the Bureau of Industry and Security (BIS) greatly reconsider the specialized treatment of "600 series" products and technologies and remove the proposed requirements in order for the "600 series" to be in line with the rest of the Commerce Control List (CCL). As currently proposed, any perceived benefit of moving these products and technologies from the United States Munitions List (USML) to the CCL is eliminated. Below are specific examples and topics that are offered to BIS for consideration prior to Final Rule publication.

(a) Automated Export System (AES) Filings

The proposed §758.1(b)(3) requires all "600 series" items to be subject to AES entry filings at all times. We believe this will have a burdensome effect and cause confusion for companies that export other non "600 series" CCL products. The shift to the CCL of certain USML controlled products consisted of an expectation that exporting the "600 series" products would fall under current EAR practices as outlined in §758. The rationale for breaking from current requirements under the EAR is unclear. This new path could have a negative impact on how exporters currently process their exports. Consider that the requirements for AES filings are currently not driven by ECCN classification but rather by a product's Schedule B or Harmonized Tariff Schedule (HTSUS) code, license coverage, or destination. One specific point of confusion will rest in the AES exception surrounding exports of like items with the same Schedule B or HTSUS code when the total value is less than $2,500 (15 CFR Part 30.37). A scenario for consideration is that a company has a shipment of a "600 series" product which has the same Schedule B or HTSUS code as a non "600 series" product. The combined value of both products is $1,000. Today, that shipment would not require AES filing. Under the proposed changes, it would require a filing. The purpose and benefit to BIS in treating "600 series" products differently as shown in the example scenario is unclear and at a cost to industry not currently realized. In order to ensure that AES filings are occurring for the different levels of control under the EAR, companies could be required to establish an internal system that would separate the export shipments of any "600 series" product from any other CCL controlled product. BIS could be setting things in motion to establish a third controlling regime requiring its own special internal company controls.

It is our assertion that industry will incur administrative costs with the specialized treatment of "600 series" products. Industry will have a more difficult time combining shipments of "600 series" products and non "600 series" products. Most companies currently split their ITAR and EAR shipments to best complete the required fields in AES. Many, in order to ensure compliance with the proposed regulations, will separate out "600 series" shipments as well. There would now exist essentially a third controlling regime to oversee separate AES filings which yields no added benefit to the exporter; only additional costs.

1. USML
2. CCL non "600 series"
3. CCL "600 series"

(b) Destination Control Statement

Continuing with the same discussion points on AES filing requirements identified above, the same burden is realized in the requirement for a special destination control statement (DCS) for "600 series" products. This is a requirement to include different language than that which is currently required by the EAR for all other CCL controlled products. We assert that this special treatment ensures that industry will be required to establish a third system of controls for its

products. An exporter would have great difficulty combining a shipment with both "600 series" products and non "600 series" products as the paperwork would have two DCS citations applied. If the products are not separated out for export shipping paperwork processing, the potential for industry to misapply the appropriate DCS to a shipment is great, ultimately leading to an increase in administrative violations of the EAR which could impact a company with fines and penalties. To protect against these fines and penalties, industry will be more likely to implement gates and processes to accommodate this third controlling regime for the processing of "600 series" export shipments.

The added administrative and cost burden for an exporter to process these different AES filings and prepare three separate shipments each with their own DCS is immeasurable as each company processes shipments differently. However, the following provides examples which amplify the burden rate that could outlast the two year phased implementation period[1]:

- Time necessary to prepare separate shipping documents for products going to the same end user, same end use, and fall under the same Schedule B or HTSUS,
- Boxing and packaging products separately,
- Arranging additional cargo space on shipment routes,
- Added shipping charges to cover the separate packages, and
- Costs and additional fees to freight forwarders for filing separate AES records.

HII recommends that BIS eliminate the requirements at §758.1(b)(3) - (b)(4) and rely upon the existing AES filing requirements as currently outlined in the EAR and by Census. Furthermore, the proposed DCS language does not appear to offer any additional benefits to the current DCS found at §758.6. Implementing a second DCS for "600 series" products is too burdensome and unnecessary. HII recommends that BIS eliminate the requirements at §758.6(b).

II. Foreign Supply Chain Activity

As background, HII builds nuclear and non-nuclear military vessels that will clearly stay on the USML following the effective date of the export reform. However, these vessels are built with many vendor furnished systems and components that will move to the CCL. If foreign vendors are involved, they can be expected, depending upon their product, to participate in the installation or integration of their parts into the vessel. HII currently manages the majority of its supply chain activity under Technical Assistance Agreements (TAAs). This represents the preponderance of HII's export activity and is applicable to roughly 75% of its current export authorizations. In reviewing the transition plan details of both the Directorate of Defense Trade Controls (DDTC) and BIS, and the overall export control reform initiative, it has been

[1] There could be upfront costs associated with establishing a third control system which might include IT modifications to software programs and databases and retraining of personnel.

interpreted that HII, through its normal foreign supply chain activity, will be subjected to double licensing. The following information expands upon this interpretation and provides details for which both DDTC and BIS should consider as it moves towards a Final Rule.

(a) The Scenario

This supply chain scenario contemplates incorporating a CCL item into a USML item. This is a very real scenario as we expect many ship systems to transition from the ITAR to the CCL. An anticipated example under this scenario is the incorporation of a CCL part or component captured at ECCN 8A609.x into a USML vessel controlled at Category VI(a). In order to install/integrate the CCL part or component, data related to the military vessel must be shared for proper installation. This would create an export of USML Category VI(e) data and services. Additionally, installation of the part or component would thereby create an export of data controlled by ECCN 8E609.a.

(b) Double Licensing

Based upon the proposed changes to the EAR, we have interpreted that this scenario will require both a license/agreement from DDTC to cover the integration information and services related to the USML controlled vessel and a license from BIS to cover the installation of the CCL controlled part/component.

Possible license exception – STA §740.20. It was our understanding that the Strategic Trade Authorization (STA) license exception would be used in the majority of "600 series" exports. Clarification is still required to outline how STA could be used for many "600 series" exports. Specifically, in reviewing §740.20(c)(1), note that this section does not appear to apply to ECCNs that also have AT controls. This would eliminate any product or technology captured by the proposed ECCNs 8A609 and 8E609. STA could not be utilized. Note also that the proposed language in the Note 2 to paragraph (c) allows for use of STA if DDTC or BIS have issued a license to the same purchaser, intermediate consignee, ultimate consignee and end user. However, the proposed (d)(2) language related to "600 series" identifies that the only eligible foreign parties are foreign governments. It would appear that foreign vendors would not be eligible end users under STA even if prior export approvals had been obtained from DDTC or BIS. By keeping the eligible foreign parties to only foreign governments, the exception for foreign supply chain activities would not apply, meaning a license will be needed for all foreign suppliers of "600 series" piece parts, components and accessories as no other exception appears to be available to cover this activity. If interpreted correctly, this would appear to be the same level of coverage as currently applied by the ITAR, the least significant part or component is generally controlled the same way as the most significant part or component and the end item itself.

(c) Additional Detail on the Supply Chain Scenario

To elaborate on the supply chain scenario further, Federal Register Notice of Proposed Rule RIN 1400-AC80 was published on April 13, 2011 that related to a revised definition of defense services. The proposed revisions included new language at §120.9(a)(2) which comprised the "integration" of items, whether controlled by the USML or the CCL, into USML controlled defense articles even if ITAR-controlled "technical data" is not provided to a foreign person during the provision of the services.

We do not know the status of this proposed rule but have reviewed the transition guidance against the proposed new defense services definition. Clarification will be required to coordinate BIS' transition plan and DDTC's policy statement with the proposed new definition and its relationship to installing "600 series" parts into USML items. DDTC's policy statement regarding Returning Without Action any license or agreement submission that incorporates a CCL item will need more explanation.

It is HII's interpretation that DDTC was moving away from controlling products and technologies at the basic level as it applies to operation, installation, maintenance and repair. Specifically, DDTC proposed in its Federal Register Notice of Proposed Rule the removal of overly broad export coverage and proposed eliminating certain forms of assistance and services that no longer warranted export control under the ITAR. HII recommends that BIS follow in this movement toward the removal of overly broad coverage and eliminate from "600 series" Category E ECCN headers (e.g., ECCN 8E609) the words "operation, installation, maintenance, repair or overhaul" and replace with the word "use". Furthermore, the removal of such coverage would eliminate the licensing requirement outlined above as the installation of those parts would not be subject to export control under the EAR. This in turn would no longer result in double licensing.

(d) Unforeseen Negative Impact if Interpretation is Correct

The burden associated with double licensing of such a scenario cannot be understated. Not only would we be tasked with identifying and obtaining the appropriate licenses from the corresponding regulatory agencies, we also would be subjected to administering two licenses and implementing two sets of regulatory rules for one installation event. This is untenable considering the differing limitations and provisos each regulatory agency could apply to their licenses for the same activity and each regulation's strict adherence requirements to record keeping.

We see a particularly heavy burden for companies like HII that utilize internal electronic approval and record keeping systems. Under the supply chain scenario described above, each time an export is contemplated, an internal company request is generated for approval. Since HII employees will now operate under two separate license authorizations, they would be required to

enter two export requests in the electronic system; one for each license. Consequently, it would task the export compliance professionals to review and approve two requests in order to administer both licenses. Please keep in mind that even if by chance the CCL part or component happened to be captured by ECCN 8A609.y, installation is still covered and the related data is still captured at ECCN 8E609.y. The lower level controls would make the data eligible for No License Required (NLR) export coverage; however, even NLR exports require a record to be maintained. The administration and record keeping burdens are not lessened by the alleviation of a formal export license approval from BIS.

Implementing the proposed changes to the export control system would be tantamount to doubling the current workload of export compliance professionals who work in a foreign supply chain business model and manufacture USML controlled products. HII and like companies would be subjected to large increases in licenses to manage and would most likely be required to hire more staff to implement the changes and manage the proposed export control system far beyond the two year phased implementation period.

Not only could the double licensing cause a significant burden, it could confuse foreign parties as to how they are to properly control the data they are receiving. For instance, the installation and corresponding data described above would be delivered under an approved license from BIS. That license might be issued with a proviso that requires formal notification to the foreign party that they'd be receiving data under the CCL. While at the same time of providing formal notification to comply with the BIS license, they'd be presented with a TAA for signature that incorporates ITAR control requirements. Asking that foreign parties grasp and understand the distinctions between U.S. export control coverage of the data they receive in this supply chain scenario can lead to confusion and a lack of clarity. Greater risks surface for the foreign party when re-exporting or retransferring the data under the wrong regulation.

We are still reviewing the potential impact of items changing controls to BIS that have related drawings and documents which contain markings dictated by our U.S. Navy contractual terms and DD 254 requirements. There is a potential that a BIS license proviso marking requirement, exception marking requirements or the general DCS under the EAR may be in direct conflict with contractual marking requirements. We will continue to explore the breadth of this issue and suggest that DDTC and BIS consult with the Department of Defense in order to provide clarification in the Final Rule. Contrary markings could also lead to confusion by a foreign party and result in inappropriate treatment as described in the last paragraph.

Lastly, the burden is not industries' alone. Both DDTC and BIS licensing officers' workload would not be lessened in this scenario.

As this supply chain scenario is a very common one at HII, we request thoughtful consideration be made to not have industry double license its export activity for installation and integration of CCL captured products into USML platforms or systems.

III. Validity Periods

We applaud BIS' attempt at aligning export authorization validity periods that coincide with TAAs, and anticipate the case-by-case review of extended expiration dates will be approved with no issues.

IV. Exceptions

(a) §740.2 Restrictions

HII suggests combining the language of §740.2(a)(6) with the (a)(12) proposed language as they are very similar. Their separation could cause confusion. We also note that the countries listed in the proposed §740.2(a)(12) section are more inclusive than just 22 CFR 126.1(a) countries. The proposed language includes all 126.1 countries. As described in the Background information of the Federal Register Notice, the intent was to focus on 126.1(a) countries. HII suggests BIS provide clarification in the Final Rule regarding the scope of control relative to 126.1 countries.

(b) §740.9 TMP

Section §740.9(a)(3)(A) proposes the use of TMP if the export would otherwise be eligible under an existing license or the export would be NLR applicable. Clarification is requested to explain the rationale for TMP usage when a license is already obtained. Also, please explain the need to use TMP when the export is NLR and does not rise to the control level of being eligible to use an exception. This appears to be contrary to the EAR Decision Tree found at Supplement No. 1 to Part 732.

(c) §740.11 GOV

Section §740.11(b)(iii)(G) requires the inclusion of a statement on shipping paperwork stating that the US Government owns the property being exported. This may not always be the case and is currently not required by the ITAR. Requirement of this statement may make this exception unusable and result in additional export licenses where currently none are required. Suggest removing statement requirement; the DCS and EEI references should be sufficient.

V. Implementation Timeline

Although the transition plan allows for the continued use of existing export authorizations for a two year period, HII requests a 180 day window prior to effective date of the export reforms. Reasons behind this request are outlined below;

- Requirement to make company purchases. As previously identified, HII utilizes an automated solution to support its export compliance program. We will be required to purchase additional software packages or make edits to existing internal software databases that relate to internal company export controls in order to comply with the proposed changes. As many within the defense industry utilize the same software providers, they may not be able to accommodate each company's needs within a shorter timeframe.
- Requirement to update procedures. Export compliance procedures, work instructions and applicable forms will need to be reviewed for impact. Some will require editing and republishing.
- Requirement for extensive training. We also would require the time necessary to train and educate the various organizations within our company to ensure full compliance with the Final Rule. Particularly those employees who provide technical expertise to our compliance program and who support jurisdiction determinations. They will need to be retrained on how to approach jurisdiction and classification.
- Requirement to review existing jurisdiction classifications. HII has a database of almost 6,000 line items including parts, components, software and technologies that will need to be reviewed for impact against the proposed changes to determine if jurisdiction has indeed moved to the EAR or remains ITAR controlled.
- Requirement to review staffing levels. Due to the possible doubling of export compliance workload as a result of the proposed regulatory changes, a review will be needed to identify if current staffing levels will be able to handle the influx of duties. The hiring of new personnel will take time to put into effect.

HII, along with many companies, have provided BIS comments for consideration which could greatly change what has been proposed for the overall export reform initiative. With that being said, we are unable to predict which recommendations BIS will accept. Therefore, we cannot effectively plan for the final outcome. It is our assertion that immediate implementation of the reforms could result in our company not being able to effectively comply in the short term. We ask for a reasonable time to best accommodate the export reform changes.

VI. Final Comments

Export control reform is a monumental task focused on shoring up controls surrounding our nation's most sensitive technologies. We recognize the hard work and attention that BIS has devoted to this effort; however, the resulting proposed regulatory changes have generated many questions and concerns about interpretation and application to everyday business. Additional clarification will be needed and we respectfully request that BIS publish a second draft of the transition plan for further review and not immediately issue a Final Rule.

We appreciate the opportunity to outline an export scenario which applies to many aerospace and defense companies. Our interpretation of the proposed changes would lead to double licensing of our foreign supply chain activity. Any clarification BIS can provide to counter that interpretation is much appreciated.

The Federal Register Notice Background section identifies that movement to the CCL of items that do not warrant USML control will result in three enhancements to national security; easing of foreign supply channels in support of manufacturing U.S. military products was not reflected. As a manufacturer of U.S. Navy and Coast Guard vessels, we ask that BIS consider export activity in a foreign supply chain arrangement to be as equally important to our nation's security. We offer that national security interests would be further served with a streamlined foreign supply chain accessible to the aerospace and defense industry.

If you have any questions regarding these comments, please contact me at (228) 935-0518 or at sandra.cross@hii-co.com.

Sincerely,

Sandra R Cross
Corporate Director, International Trade Compliance
Huntington Ingalls Industries, Inc.