

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

FORM 10-Q

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2019
or

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934**

Commission file number 001-34910

HUNTINGTON INGALLS INDUSTRIES, INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

90-0607005

(I.R.S. Employer
Identification No.)

4101 Washington Avenue Newport News, Virginia 23607

(Address of principal executive offices and zip code)

(757) 380-2000

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class

Trading Symbol(s)

Name of each exchange on which registered

Common Stock

HII

New York Stock Exchange

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer ☒

Non-Accelerated Filer ☐

Accelerated Filer ☐

Smaller Reporting Company ☐

Emerging Growth Company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

As of November 1, 2019, 40,900,357 shares of the registrant's common stock were outstanding.

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HUNTINGTON INGALLS INDUSTRIES, INC.
PART I - FINANCIAL INFORMATION
Item 1. Financial Statements
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (UNAUDITED)

(in millions, except per share amounts)	Three Months Ended September 30		Nine Months Ended September 30	
	2019	2018	2019	2018
Sales and service revenues				
Product sales	\$ 1,545	\$ 1,547	\$ 4,555	\$ 4,416
Service revenues	674	536	1,932	1,561
Sales and service revenues	2,219	2,083	6,487	5,977
Cost of sales and service revenues				
Cost of product sales	1,246	1,159	3,754	3,369
Cost of service revenues	556	434	1,634	1,287
Income from operating investments, net	6	8	15	12
Other income and gains	—	—	—	14
General and administrative expenses	209	208	564	609
Operating income	214	290	550	738
Other income (expense)				
Interest expense	(18)	(14)	(52)	(44)
Non-operating retirement benefit	3	19	8	56
Other, net	(1)	—	5	2
Earnings before income taxes	198	295	511	752
Federal and foreign income taxes	44	66	111	128
Net earnings	\$ 154	\$ 229	\$ 400	\$ 624
Basic earnings per share	\$ 3.74	\$ 5.29	\$ 9.66	\$ 14.15
Weighted-average common shares outstanding	41.2	43.3	41.4	44.1
Diluted earnings per share	\$ 3.74	\$ 5.29	\$ 9.66	\$ 14.15
Weighted-average diluted shares outstanding	41.2	43.3	41.4	44.1
Dividends declared per share	\$ 0.86	\$ 0.72	\$ 2.58	\$ 2.16
Net earnings from above	\$ 154	\$ 229	\$ 400	\$ 624
Other comprehensive income				
Change in unamortized benefit plan costs	25	20	74	61
Other	1	—	1	(2)
Tax expense for items of other comprehensive income	(7)	(5)	(19)	(16)
Other comprehensive income, net of tax	19	15	56	43
Comprehensive income	\$ 173	\$ 244	\$ 456	\$ 667

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

HUNTINGTON INGALLS INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION (UNAUDITED)

(\$ in millions)	September 30 2019	December 31 2018
Assets		
Current Assets		
Cash and cash equivalents	\$ 32	\$ 240
Accounts receivable, net of allowance for doubtful accounts of \$4 million as of 2019 and \$9 million as of 2018	489	252
Contract assets	1,218	1,003
Inventoried costs, net	139	128
Prepaid expenses and other current assets	147	122
Total current assets	2,025	1,745
Property, plant, and equipment, net of accumulated depreciation of \$1,935 million as of 2019 and \$1,829 million as of 2018	2,700	2,517
Operating lease assets	208	—
Goodwill	1,402	1,263
Other intangible assets, net of accumulated amortization of \$599 million as of 2019 and \$564 million as of 2018	506	492
Deferred tax assets	102	163
Miscellaneous other assets	241	203
Total assets	\$ 7,184	\$ 6,383
Liabilities and Stockholders' Equity		
Current Liabilities		
Trade accounts payable	\$ 616	\$ 562
Accrued employees' compensation	299	248
Current portion of postretirement plan liabilities	131	131
Current portion of workers' compensation liabilities	228	225
Contract liabilities	344	331
Other current liabilities	332	332
Total current liabilities	1,950	1,829
Long-term debt	1,549	1,283
Pension plan liabilities	749	764
Other postretirement plan liabilities	345	348
Workers' compensation liabilities	455	454
Long-term operating lease liabilities	172	—
Other long-term liabilities	259	189
Total liabilities	5,479	4,867
Commitments and Contingencies (Note 16)		
Stockholders' Equity		
Common stock, \$0.01 par value; 150 million shares authorized; 53.2 million shares issued and 41.0 million shares outstanding as of September 30, 2019, and 53.1 million shares issued and 41.9 million shares outstanding as of December 31, 2018	1	1
Additional paid-in capital	1,950	1,954
Retained earnings	2,902	2,609
Treasury stock	(1,916)	(1,760)
Accumulated other comprehensive loss	(1,232)	(1,288)
Total stockholders' equity	1,705	1,516
Total liabilities and stockholders' equity	\$ 7,184	\$ 6,383

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

HUNTINGTON INGALLS INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(\$ in millions)	Nine Months Ended September 30	
	2019	2018
Operating Activities		
Net earnings	\$ 400	\$ 624
Adjustments to reconcile to net cash provided by (used in) operating activities		
Depreciation	126	129
Amortization of purchased intangibles	35	28
Amortization of debt issuance costs	2	3
Provision for doubtful accounts	(5)	(4)
Stock-based compensation	19	27
Deferred income taxes	42	(1)
Change in		
Accounts receivable	(223)	(33)
Contract assets	(197)	(280)
Inventoried costs	(14)	3
Prepaid expenses and other assets	(62)	5
Accounts payable and accruals	147	230
Retiree benefits	56	(468)
Other non-cash transactions, net	4	3
Net cash provided by operating activities	330	266
Investing Activities		
Capital expenditures		
Capital expenditure additions	(349)	(293)
Grant proceeds for capital expenditures	71	33
Acquisitions of businesses, net of cash received	(195)	—
Investment in affiliates	—	(10)
Proceeds from disposition of assets	—	3
Other investing activities, net	3	—
Net cash used in investing activities	(470)	(267)
Financing Activities		
Proceeds from revolving credit facility borrowings	5,048	—
Repayment of revolving credit facility borrowings	(4,784)	—
Dividends paid	(107)	(95)
Repurchases of common stock	(202)	(512)
Employee taxes on certain share-based payment arrangements	(23)	(25)
Net cash used in financing activities	(68)	(632)
Change in cash and cash equivalents	(208)	(633)
Cash and cash equivalents, beginning of period	240	701
Cash and cash equivalents, end of period	\$ 32	\$ 68
Supplemental Cash Flow Disclosure		
Cash paid for income taxes	\$ 124	\$ 77
Cash paid for interest	\$ 40	\$ 32
Non-Cash Investing and Financing Activities		
Capital expenditures accrued in accounts payable	\$ 12	\$ 7
Accrued repurchases of common stock	\$ 2	\$ 2

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

HUNTINGTON INGALLS INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY (UNAUDITED)

Three Months Ended September 30, 2019 and 2018 (\$ in millions)	Common Stock	Additional Paid-in Capital	Retained Earnings (Deficit)	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balance as of June 30, 2018	\$ 1	\$ 1,932	\$ 2,236	\$ (1,385)	\$ (1,085)	\$ 1,699
Net earnings	—	—	229	—	—	229
Dividends declared (\$0.72 per share)	—	—	(31)	—	—	(31)
Stock compensation	—	12	—	—	—	12
Other comprehensive income, net of tax	—	—	—	—	15	15
Treasury stock activity	—	—	—	(99)	—	(99)
Balance as of September 30, 2018	<u>\$ 1</u>	<u>\$ 1,944</u>	<u>\$ 2,434</u>	<u>\$ (1,484)</u>	<u>\$ (1,070)</u>	<u>\$ 1,825</u>
Balance as of June 30, 2019	\$ 1	\$ 1,943	\$ 2,783	\$ (1,848)	\$ (1,251)	\$ 1,628
Net earnings	—	—	154	—	—	154
Dividends declared (\$0.86 per share)	—	—	(35)	—	—	(35)
Stock compensation	—	7	—	—	—	7
Other comprehensive income, net of tax	—	—	—	—	19	19
Treasury stock activity	—	—	—	(68)	—	(68)
Balance as of September 30, 2019	<u>\$ 1</u>	<u>\$ 1,950</u>	<u>\$ 2,902</u>	<u>\$ (1,916)</u>	<u>\$ (1,232)</u>	<u>\$ 1,705</u>
Nine Months Ended September 30, 2019 and 2018 (\$ in millions)	Common Stock	Additional Paid-in Capital	Retained Earnings (Deficit)	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balance as of December 31, 2017	\$ 1	\$ 1,942	\$ 1,687	\$ (972)	\$ (900)	\$ 1,758
Net earnings	—	—	624	—	—	624
Dividends declared (\$2.16 per share)	—	—	(95)	—	—	(95)
Stock compensation	—	2	—	—	—	2
Other comprehensive income, net of tax	—	—	—	—	43	43
Treasury stock activity	—	—	—	(512)	—	(512)
Effect of Accounting Standards Update 2014-09	—	—	5	—	—	5
Effect of Accounting Standards Update 2016-01	—	—	11	—	(11)	—
Effect of Accounting Standards Update 2018-02	—	—	202	—	(202)	—
Balance as of September 30, 2018	<u>\$ 1</u>	<u>\$ 1,944</u>	<u>\$ 2,434</u>	<u>\$ (1,484)</u>	<u>\$ (1,070)</u>	<u>\$ 1,825</u>
Balance as of December 31, 2018	\$ 1	\$ 1,954	\$ 2,609	\$ (1,760)	\$ (1,288)	\$ 1,516
Net earnings	—	—	400	—	—	400
Dividends declared (\$2.58 per share)	—	—	(107)	—	—	(107)
Stock compensation	—	(4)	—	—	—	(4)
Other comprehensive income, net of tax	—	—	—	—	56	56
Treasury stock activity	—	—	—	(156)	—	(156)
Balance as of September 30, 2019	<u>\$ 1</u>	<u>\$ 1,950</u>	<u>\$ 2,902</u>	<u>\$ (1,916)</u>	<u>\$ (1,232)</u>	<u>\$ 1,705</u>

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

HUNTINGTON INGALLS INDUSTRIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. DESCRIPTION OF BUSINESS

Huntington Ingalls Industries, Inc. ("HII" or the "Company") is one of America's largest military shipbuilding companies and a provider of professional services to partners in government and industry. HII is organized into three reportable segments: Ingalls Shipbuilding ("Ingalls"), Newport News Shipbuilding ("Newport News"), and Technical Solutions. For more than a century, the Company's Ingalls segment in Mississippi and Newport News segment in Virginia have built more ships in more ship classes than any other U.S. naval shipbuilder. The Technical Solutions segment provides a range of services to the governmental, energy, and oil and gas markets.

HII conducts most of its business with the U.S. Government, primarily the Department of Defense ("DoD"). As prime contractor, principal subcontractor, team member, or partner, the Company participates in many high-priority U.S. defense technology programs. Through its Ingalls segment, HII is a builder of amphibious assault and expeditionary ships for the U.S. Navy, the sole builder of National Security Cutters for the U.S. Coast Guard, and one of only two companies that builds the Navy's current fleet of *Arleigh Burke* class (DDG 51) destroyers. Through its Newport News segment, HII is the nation's sole designer, builder, and refueler of nuclear-powered aircraft carriers, and one of only two companies currently designing and building nuclear-powered submarines for the U.S. Navy. The Technical Solutions segment provides a wide range of professional services, including fleet support, mission driven innovative solutions ("MDIS"), nuclear and environmental, and oil and gas services.

2. BASIS OF PRESENTATION

Principles of Consolidation - The unaudited condensed consolidated financial statements of HII and its subsidiaries have been prepared in conformity with accounting principles generally accepted in the United States of America ("GAAP") and the instructions to Form 10-Q promulgated by the Securities and Exchange Commission ("SEC"). All intercompany transactions and balances are eliminated in consolidation. For classification of current assets and liabilities related to its long-term production contracts, the Company uses the duration of these contracts as its operating cycle, which is generally longer than one year. Additionally, certain prior year amounts have been reclassified to conform to the current year presentation.

These unaudited condensed consolidated financial statements include all adjustments of a normal recurring nature considered necessary by management for a fair presentation of the unaudited condensed consolidated financial position, results of operations, and cash flows and should be read in conjunction with the Company's audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2018.

The quarterly information is labeled using a calendar convention; that is, first quarter is consistently labeled as ending on March 31, second quarter as ending on June 30, and third quarter as ending on September 30. It is management's long-standing practice to establish interim closing dates using a "fiscal" calendar, which requires the businesses to close their books on a Friday near these quarter-end dates in order to normalize the potentially disruptive effects of quarterly closings on business processes. The effects of this practice only exist for interim periods within a reporting year.

Government Grants - The Company recognizes incentive grants, inclusive of transfers of depreciable assets, from federal, state, and local governments at fair value upon compliance with the conditions of their receipt and reasonable assurance that the grants will be received or the depreciable assets will be transferred. Grants in recognition of specific expenses are recognized in the same period as an offset to those related expenses. Grants related to depreciable assets are recognized over the periods and in the proportions in which depreciation expense on those assets is recognized.

For the nine months ended September 30, 2019, the Company recognized cash grant benefits of approximately \$71 million in other long-term liabilities in the unaudited condensed consolidated statements of financial position. For the nine months ended September 30, 2018, the Company recognized cash grant benefits of approximately \$33 million in other long-term liabilities in the unaudited condensed consolidated statements of financial position.

Fair Value of Financial Instruments - Except for the Company's long-term debt, the carrying amounts of the Company's financial instruments recorded at historical cost approximate fair value due to the short-term nature of the instruments and low credit risk associated with the respective counterparties.

The Company maintains multiple grantor trusts to fund certain non-qualified pension plans. These trusts were valued at \$136 million and \$109 million as of September 30, 2019, and December 31, 2018, respectively, and are presented within miscellaneous other assets within the unaudited condensed consolidated statements of financial position. These trusts consist primarily of investments in marketable securities, which are held at fair value within Level 1 of the fair value hierarchy.

Leases - The Company determines if an arrangement is a lease at contract inception. A lease exists when a contract conveys to a party the right to control the use of identified property, plant, or equipment for a period of time in exchange for consideration. The Company recognizes a lease liability at the lease commencement date, as the present value of future lease payments, using an estimated rate of interest that the Company would pay to borrow equivalent funds on a collateralized basis. A lease asset is recognized based on the lease liability value and adjusted for any prepaid lease payments, initial direct costs, or lease incentive amounts. The lease term at the commencement date includes any renewal options or termination options when it is reasonably certain that the Company will exercise or not exercise those options, respectively.

Right of use assets associated with operating leases are recognized in operating lease assets in the unaudited condensed consolidated statements of financial position. Lease liabilities associated with operating leases are recognized in long-term operating lease liabilities, with short-term lease liability amounts included in other current liabilities in the unaudited condensed consolidated statements of financial position.

Rent expense for operating leases is recognized on a straight-line basis over the lease term and included in cost of sales and service revenues on the unaudited condensed consolidated statements of operations and comprehensive income. Variable lease payments are recognized as incurred and include lease operating expenses, which are based on contractual lease terms.

The Company elected to exclude from its unaudited condensed consolidated statements of financial position leases having terms of 12 months or less (short-term leases) and elected not to separate lease and non-lease components in the determination of lease payment obligations for its long-term lease contracts.

Loan Receivable - The Company holds a loan receivable in connection with a seller financed transaction involving its previously owned Avondale shipyard facility. The receivable is carried at amortized cost in the amount of \$39 million, net of a \$9 million loan discount, which approximates fair value and is recorded in miscellaneous other assets on the unaudited condensed consolidated statements of financial position. Interest income is recognized on an accrual basis using the effective yield method. The discount is accreted into income using the effective yield method over the estimated life of the loan receivable.

Related Party Transactions - On March 29, 2011, HII entered into a Separation and Distribution Agreement (the "Separation Agreement") with its former parent company, Northrop Grumman Corporation ("Northrop Grumman"), and Northrop Grumman's subsidiaries (Northrop Grumman Shipbuilding, Inc. and Northrop Grumman Systems Corporation), pursuant to which HII was legally and structurally separated from Northrop Grumman. For the year ended December 31, 2018, the Company received \$8 million from Northrop Grumman under the Separation Agreement. The Company had \$84 million outstanding under Industrial Revenue Bonds issued by the Mississippi Business Finance Corporation as of each of September 30, 2019, and December 31, 2018. Prior to the spin-off, repayment of principal and interest was guaranteed by Northrop Grumman Systems Corporation. The guaranty remains in effect, and the Company has agreed to indemnify Northrop Grumman Systems Corporation for any losses related to the guaranty.

3. ACCOUNTING STANDARDS UPDATES

In February 2016, the FASB issued ASU 2016-02, "Leases (Topic 842)," which established a right-of-use model that requires a lessee to record the right-of-use asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Expense is recognized in the income statement similar to the recognition of expense under previous accounting guidance. Additional qualitative and quantitative disclosures are required. ASU 2016-02 was effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Prior to the FASB issuing ASU 2018-11 "Leases (Topic 842): Targeted Improvements," entities were required to use

a modified retrospective approach upon adoption to recognize and measure leases at the beginning of the earliest comparative period presented in the financial statements. In January 2018, the FASB issued ASU 2018-01 "Leases (Topic 842): Land Easement Practical Expedient for Transition to Topic 842," which permitted entities to forgo the evaluation of existing land easement arrangements to determine if they contain a lease as part of the adoption of ASU 2016-02 issued in February 2016. Accordingly, the Company's accounting treatment of any existing land easement arrangements has not changed. The Company adopted this standard update concurrently with ASU 2016-02. In July 2018, the FASB issued ASU 2018-11, which provides entities the option to initially apply ASU 2016-02 at the adoption date and recognize a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. Consequently, the comparative periods presented in the financial statements would continue to comply with current GAAP.

The Company adopted ASU 2016-02 on January 1, 2019, using the optional transition method. In addition, the Company elected practical expedients permitted under the transition guidance within the new standard, which, among other things, allows it to carry forward historical lease classifications. The Company also elected the hindsight practical expedient to determine the reasonably certain lease term for existing leases. The Company's election of the hindsight practical expedient resulted in lengthening lease terms for certain existing leases. The Company made an accounting policy election not to recognize leases with an initial term of 12 months or less in the unaudited condensed consolidated statements of financial position and to recognize the lease payments in the unaudited condensed consolidated statements of operations and comprehensive income on a straight-line basis over the lease terms. The impact upon adoption was an increase to operating lease assets of \$215 million, an increase to short-term operating lease liabilities of \$36 million, an increase to long-term operating lease liabilities of \$179 million, and no material impact to retained earnings.

In August 2018, the FASB issued ASU 2018-13, "Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement," which changes the fair value measurement disclosure requirements of ASC 820. The update includes changes to disclosures regarding valuation techniques and inputs, uncertainty, judgments, and assumptions in fair value measurements, and how changes in fair value measurements affect performance and cash flows. The update is effective for annual reporting periods beginning after December 15, 2019, including interim periods therein. Early adoption is permitted for any eliminated or modified disclosures. The Company is currently evaluating the impact of ASU 2018-13 on its consolidated financial statements and disclosures, accounting processes, and internal controls.

In August 2018, the FASB issued ASU 2018-14, "Compensation—Retirement Benefits—Defined Benefit Plans—General (Subtopic 715-20): Disclosure Framework—Changes to the Disclosure Requirements for Defined Benefit Plans," which reduces disclosure requirements of Subtopic 715-20 and requires additional disclosure related to weighted-average interest crediting rates and significant gains and losses related to changes in the benefit obligation for the reporting period. The update is effective on a retrospective basis for fiscal years ending after December 15, 2020, with early adoption allowed. The Company is currently evaluating the impact of ASU 2018-14 on its consolidated financial statements and disclosures, accounting processes, and internal controls.

Other accounting pronouncements issued but not effective until after December 31, 2019, are not expected to have a material impact on the Company's consolidated financial position, results of operations, or cash flows.

4. AVONDALE AND GULFPORT

In August and October 2014, the Company completed closure of its Gulfport Composite Center of Excellence in Gulfport, Mississippi and ceased shipbuilding construction operations at its Avondale, Louisiana facility, respectively.

In connection with winding down shipbuilding at its Avondale facility, the Company incurred and paid related restructuring and shutdown costs. Pursuant to applicable provisions of the FAR and CAS for the treatment of restructuring and shutdown related costs, the Company began amortizing the deferred costs over five years in 2014. In November 2017, the U.S. Government and the Company reached a settlement to treat \$251 million of these costs as allowable costs, a majority of which were billed to the U.S. Government and collected by the end of 2018. The settlement was consistent with management's cost recovery expectations and did not have a material effect on the Company's statements of financial position or results of operations. In October 2018, the Company completed a sale of the Avondale facility. In addition to cash proceeds, the Company financed a portion of the transaction over nine years, resulting in a net gain of \$7 million, recognized as a reduction to cost of sales in the fourth quarter of 2018.

In connection with the closure of its Gulfport facility, the Company incurred restructuring related costs of \$54 million, including \$52 million of accelerated depreciation of fixed assets. The Company reached a resolution with the U.S. Government in December 2018 regarding the treatment and allocation of the restructuring related costs, which was substantially in accordance with management's cost recovery expectations and did not have a material effect on the Company's consolidated financial position, results of operations, or cash flows.

5. ACQUISITIONS

On February 25, 2019, the Company acquired Fulcrum IT Services, LLC ("Fulcrum"), an information technology and government consulting company, for approximately \$195 million in cash, net of \$1 million of acquired cash. The acquisition was consistent with the Company's strategy to optimize and expand its services portfolio. In connection with this acquisition, the Company recorded \$133 million of goodwill, which includes the value of Fulcrum's workforce, all of which was allocated to its Technical Solutions segment, as well as \$49 million of intangible assets related to existing contract backlog. For the nine months ended September 30, 2019, the Company recorded a decrease in goodwill of \$1 million, primarily driven by the finalization of a net working capital adjustment. The Company has not completed the purchase price allocation, because the fair value calculations for certain assets and liabilities have not been finalized. See Note 11: Goodwill and Other Intangible Assets. The assets, liabilities, and results of operations of Fulcrum are not material to the Company's consolidated financial position, results of operations, or cash flows.

On December 3, 2018, the Company acquired G2, Inc. ("G2"), a provider of cybersecurity solutions to the U.S. Government, for approximately \$77 million in cash, net of \$2 million of acquired cash. The acquisition was consistent with the Company's strategy to optimize and expand its services portfolio. In connection with this acquisition, the Company recorded \$46 million of goodwill, which includes the value of G2's workforce, all of which was allocated to its Technical Solutions segment, as well as \$20 million of intangible assets related to existing contract backlog. For the nine months ended September 30, 2019, the Company recorded an increase in goodwill of \$7 million, primarily driven by the finalization of a net working capital adjustment and the fair value calculations for certain assets and liabilities. See Note 11: Goodwill and Other Intangible Assets. The assets, liabilities, and results of operations of G2 are not material to the Company's consolidated financial position, results of operations, or cash flows.

The Company funded each of these acquisitions using cash on hand and borrowings on its revolving credit facility. The acquisition costs incurred in connection with these acquisitions were not material. The operating results of these businesses have been included in the Company's consolidated results as of the respective closing dates of the acquisitions. In allocating the purchase prices of these businesses, the Company considered the estimated fair value of net tangible and intangible assets acquired, with any excess purchase price recorded as goodwill. The total amount of goodwill resulting from these acquisitions is expected to be amortizable for tax purposes. These acquisitions are not material either individually or in the aggregate, and pro forma revenues and results of operations have therefore not been provided.

6. STOCKHOLDERS' EQUITY

Treasury Stock - In November 2017, the Company's board of directors authorized an increase in the Company's stock repurchase program from \$1.2 billion to \$2.2 billion. On November 5, 2019, the Company's board of directors authorized an increase in the Company's stock repurchase program from \$2.2 billion to \$3.2 billion and an extension of the term of the program to October 31, 2024. Repurchases are made from time to time at management's discretion in accordance with applicable federal securities laws. For the nine months ended September 30, 2019, the Company repurchased 751,497 shares at an aggregate cost of \$156 million, of which approximately \$2 million was not yet settled for cash as of September 30, 2019. For the nine months ended September 30, 2019, the Company also settled for cash \$48 million of shares repurchased in the prior year. For the nine months ended September 30, 2018, the Company repurchased 2,217,629 shares at an aggregate cost of \$512 million, of which approximately \$2 million was not yet settled for cash as of September 30, 2018. For the nine months ended September 30, 2018, the Company also settled for cash \$2 million of shares repurchased in the prior year. The cost of purchased shares is recorded as treasury stock in the unaudited condensed consolidated statements of financial position.

Dividends - The Company declared cash dividends per share of \$0.86 and \$0.72 for the three months ended September 30, 2019 and 2018, respectively. The Company declared cash dividends per share of \$2.58 and \$2.16

for the nine months ended September 30, 2019 and 2018, respectively. The Company paid cash dividends totaling \$107 million and \$95 million for the nine months ended September 30, 2019 and 2018, respectively.

Accumulated Other Comprehensive Loss - Other comprehensive income (loss) refers to gains and losses recorded as an element of stockholders' equity but excluded from net earnings. The accumulated other comprehensive loss as of September 30, 2019, was comprised of unamortized benefit plan costs of \$1,228 million and other comprehensive loss items of \$4 million. The accumulated other comprehensive loss as of December 31, 2018, was comprised of unamortized benefit plan costs of \$1,283 million and other comprehensive loss items of \$5 million.

The changes in accumulated other comprehensive income (loss) by component for the three and nine months ended September 30, 2019 and 2018, were as follows:

(\$ in millions)	Benefit Plans	Other	Total
Balance as of June 30, 2018	\$ (1,080)	\$ (5)	\$ (1,085)
Other comprehensive income (loss) before reclassifications	—	—	—
Amounts reclassified from accumulated other comprehensive loss			
Amortization of prior service cost ¹	1	—	1
Amortization of net actuarial loss ¹	19	—	19
Tax expense for items of other comprehensive income	(5)	—	(5)
Net current period other comprehensive income	15	—	15
Balance as of September 30, 2018	<u>\$ (1,065)</u>	<u>\$ (5)</u>	<u>\$ (1,070)</u>
Balance as of June 30, 2019	(1,246)	(5)	(1,251)
Other comprehensive income (loss) before reclassifications	—	1	1
Amounts reclassified from accumulated other comprehensive loss			
Amortization of prior service credit ¹	(1)	—	(1)
Amortization of net actuarial loss ¹	26	—	26
Tax expense for items of other comprehensive income	(7)	—	(7)
Net current period other comprehensive income	18	1	19
Balance as of September 30, 2019	<u>\$ (1,228)</u>	<u>\$ (4)</u>	<u>\$ (1,232)</u>

(\$ in millions)	Benefit Plans	Other	Total
Balance as of December 31, 2017	\$ (906)	\$ 6	\$ (900)
Other comprehensive income (loss) before reclassifications		(2)	(2)
Amounts reclassified from accumulated other comprehensive loss			
Amortization of prior service cost ¹	2	—	2
Amortization of net actuarial loss ¹	59	—	59
Tax expense for items of other comprehensive income	(16)	—	(16)
Net current period other comprehensive income	45	(2)	43
Effect of Accounting Standards Update 2016-01 ²	—	(11)	(11)
Effect of Accounting Standards Update 2018-02 ³	(204)	2	(202)
Balance as of September 30, 2018	(1,065)	(5)	(1,070)
Balance as of December 31, 2018	(1,283)	(5)	(1,288)
Other comprehensive income (loss) before reclassifications	—	1	1
Amounts reclassified from accumulated other comprehensive loss			
Amortization of prior service credit ¹	(3)	—	(3)
Amortization of net actuarial loss ¹	77	—	77
Tax expense for items of other comprehensive income	(19)	—	(19)
Net current period other comprehensive income	55	1	56
Balance as of September 30, 2019	\$ (1,228)	\$ (4)	\$ (1,232)

¹ These accumulated comprehensive loss components are included in the computation of net periodic benefit cost. See Note 17: Employee Pension and Other Postretirement Benefits. The tax benefit associated with amounts reclassified from accumulated other comprehensive loss for the three months ended September 30, 2019 and 2018, was \$7 million and \$5 million, respectively. The tax benefit associated with amounts reclassified from accumulated other comprehensive loss for the nine months ended September 30, 2019 and 2018, was \$19 million and \$16 million, respectively.

² The Company adopted ASU 2016-01 "Financial Statements - Overall (Subtopic 825-10)" as of January 1, 2018. Accordingly, accumulated other comprehensive income of \$11 million related to available-for-sale securities, net of \$4 million tax expense, was reclassified to retained earnings.

³ The Company adopted ASU 2018-02 "Income Statement - Reporting Comprehensive Income (Topic 220)" as of January 1, 2018. Accordingly, stranded tax effects of \$202 million related to the Tax Act were reclassified to retained earnings.

7. EARNINGS PER SHARE

Basic and diluted earnings per common share were calculated as follows:

(in millions, except per share amounts)	Three Months Ended September 30		Nine Months Ended September 30	
	2019	2018	2019	2018
Net earnings	\$ 154	\$ 229	\$ 400	\$ 624
Weighted-average common shares outstanding	41.2	43.3	41.4	44.1
Net dilutive effect of stock awards	—	—	—	—
Dilutive weighted-average common shares outstanding	41.2	43.3	41.4	44.1
Earnings per share - basic	\$ 3.74	\$ 5.29	\$ 9.66	\$ 14.15
Earnings per share - diluted	\$ 3.74	\$ 5.29	\$ 9.66	\$ 14.15

Under the treasury stock method, the Company has excluded from the diluted share amounts presented above the effects of 0.3 million Restricted Performance Stock Rights ("RPSRs") for the three and nine months ended September 30, 2019 and 2018.

8. REVENUE

The following is a description of principal activities from which the Company generates its revenues. For more detailed information regarding reportable segments, see Note 9: Segment Information. For more detailed information regarding the Company's significant accounting policy for revenue, see Note 2: Basis of Presentation.

U.S. Government Contracts

The Ingalls and Newport News segments generate revenue primarily from performance under multi-year contracts with the U.S. Government, generally the U.S. Navy and U.S. Coast Guard, or prime contractors to contracts with the U.S. Government, relating to the advance planning, design, construction, repair, maintenance, refueling, overhaul, or inactivation of nuclear-powered ships and non-nuclear ships. The period over which the Company performs may extend past five years. The Technical Solutions segment also generates the majority of its revenue from contracts with the U.S. Government, including U.S. Government agencies. The Company generally invoices and receives related payments based upon performance progress no less frequently than monthly.

Shipbuilding - For most of the Company's shipbuilding contracts, the customer contracts with the Company to provide a comprehensive service of designing, procuring long-lead-time materials, manufacturing, and integrating complex equipment and technologies into a single ship or project, often resulting in a single performance obligation. Contract modifications to account for changes in specifications and requirements are recognized when approved by the customer. In the majority of circumstances, modifications do not result in additional performance obligations that are distinct from the existing performance obligations in the contract and the effects of the modifications are recognized as an adjustment to revenue on a cumulative catch-up basis. Alternatively, in instances where the performance obligations in the modifications are deemed distinct, contract modifications are accounted for prospectively.

The Company considers incentive and award fees to be variable consideration and includes in the transaction price at inception the consideration to which the Company expects to be entitled under the terms and conditions of the contract, generally estimated using a most likely amount approach. Transaction price is limited to the extent of funding allotted by the customer and available for performance, and estimated revenues represent those amounts for which the Company believes a significant reversal of revenue is not probable.

The Company recognizes revenues related to shipbuilding contracts as it satisfies the related performance obligations over time using a cost-to-cost input method to measure performance progress, which best reflects the transfer of control to the customer.

Services - The Technical Solutions segment generates revenue primarily under U.S. Government contracts from the provision of fleet support and MDIS services. Contracts generally are structured using either an Indefinite Delivery/Indefinite Quantity ("IDIQ") vehicle, under which orders are issued, or a standalone contract. Contracts may be fixed-price or cost-type, include variable consideration such as incentives and awards, and structured as task orders under an IDIQ contract vehicle or requirements contract vehicle. In either case, the Company generally performs over the course of a short-duration period and may continue to perform upon exercise of related period of performance options that are also short in duration, generally one year. The Company's performance obligations vary in nature and may be stand-ready, in which case the Company responds to the customer's needs on the basis of its demand, a recurring service, typically recurring maintenance services, or a single performance obligation that does not comprise a series of distinct services.

In determining transaction price, the Company considers incentives and other contingencies to be variable consideration and includes in the initial transaction price the consideration to which the Company expects to be entitled under the terms and conditions of the contract, generally estimated using a most likely amount approach. Transaction price is limited to the extent of funding allotted by the customer and available for performance, and estimated revenues represent those amounts for which the Company believes a significant reversal of revenue is not probable. Where a series of distinct services has been identified, the Company generally allocates variable consideration to distinct time increments of service.

The Company generally recognizes revenue as it satisfies the related performance obligations over time using a cost-to-cost input method to measure performance progress, because, even where the Company has identified a series of services, its cost incurrence pattern generally is not ratable given the complex nature of the services the Company provides. Invoices are issued and related payments are received, on the basis of performance progress, no less frequently than monthly. In addition, many of the Company's U.S. Government services contracts are time and material arrangements. As a result, the Company often utilizes the practical expedient allowing the recognition of revenue in the amount the Company invoices, which corresponds with the value provided to the customer and to which the Company is entitled to payment for performance to date.

Non-U.S. Government Contracts

Revenues generated under commercial and state and local government agency contracts are primarily derived from the provision of nuclear and environmental and oil and gas services. Non-U.S. Government contracts typically are one or two years in duration.

In determining transaction price, the Company considers incentives and other contingencies to be variable consideration and includes in the initial transaction price the consideration to which the Company expects to be entitled under the terms and conditions of the contract, generally estimated using a most likely amount approach. In the context of variable consideration, the Company limits the transaction price to amounts for which the Company believes a significant reversal of revenue is not probable. Such amounts may relate to transaction price in excess of funding, a lack of history with the customer, a lack of history with the goods or services being provided, or other items.

Revenue generally is recognized over time given the terms and conditions of the related contracts. The Company generally utilizes a cost-to-cost input method to measure performance progress, which best depicts the transfer of control to the customer. The Company's non-U.S. Government contract portfolio is comprised of a large number of time and material arrangements. As a result, the Company often utilizes the practical expedient allowing the recognition of revenue in the amount the Company invoices, which corresponds with the value provided to the customer and to which the Company is entitled to payment for performance to date.

Disaggregation of Revenue

The following tables present revenues on a disaggregated basis, in a manner that reconciles with the Company's reportable segment disclosures, for the following categories: product versus service type, customer type, contract type, and major program. See Note 9: Segment Information. The Company believes that this level of disaggregation provides investors with information to evaluate the Company's financial performance and provides the Company with information to make capital allocation decisions in the most appropriate manner.

	Three Months Ended September 30, 2019					
(\$ in millions)	Ingalls	Newport News	Technical Solutions	Intersegment Eliminations	Total	
Revenue Type						
Product sales	\$ 584	\$ 952	\$ 9	\$ —	\$ 1,545	
Service revenues	62	310	302	—	674	
Intersegment	1	2	36	(39)	—	
Sales and service revenues	\$ 647	\$ 1,264	\$ 347	\$ (39)	\$ 2,219	
Customer Type						
Federal	\$ 646	\$ 1,262	\$ 233	\$ —	\$ 2,141	
Commercial	—	—	78	—	78	
Intersegment	1	2	36	(39)	—	
Sales and service revenues	\$ 647	\$ 1,264	\$ 347	\$ (39)	\$ 2,219	
Contract Type						
Firm fixed-price	\$ 21	\$ 2	\$ 66	\$ —	\$ 89	
Fixed-price incentive	519	578	—	—	1,097	
Cost-type	106	682	125	—	913	
Time and materials	—	—	120	—	120	
Intersegment	1	2	36	(39)	—	
Sales and service revenues	\$ 647	\$ 1,264	\$ 347	\$ (39)	\$ 2,219	
	Three Months Ended September 30, 2018					
(\$ in millions)	Ingalls	Newport News	Technical Solutions	Intersegment Eliminations	Total	
Revenue Type						
Product sales	\$ 636	\$ 891	\$ 20	\$ —	\$ 1,547	
Service revenues	56	286	194	—	536	
Intersegment	2	2	31	(35)	—	
Sales and service revenues	\$ 694	\$ 1,179	\$ 245	\$ (35)	\$ 2,083	
Customer Type						
Federal	\$ 692	\$ 1,177	\$ 155	\$ —	\$ 2,024	
Commercial	—	—	59	—	59	
Intersegment	2	2	31	(35)	—	
Sales and service revenues	\$ 694	\$ 1,179	\$ 245	\$ (35)	\$ 2,083	
Contract Type						
Firm fixed-price	\$ 31	\$ 2	\$ 33	\$ —	\$ 66	
Fixed-price incentive	569	472	—	—	1,041	
Cost-type	92	703	90	—	885	
Time and materials	—	—	91	—	91	
Intersegment	2	2	31	(35)	—	
Sales and service revenues	\$ 694	\$ 1,179	\$ 245	\$ (35)	\$ 2,083	

Nine Months Ended September 30, 2019

(\$ in millions)	Ingalls	Newport News	Technical Solutions	Intersegment Eliminations	Total
Revenue Type					
Product sales	\$ 1,678	\$ 2,842	\$ 35	\$ —	\$ 4,555
Service revenues	173	950	809	—	1,932
Intersegment	2	4	96	(102)	—
Sales and service revenues	\$ 1,853	\$ 3,796	\$ 940	\$ (102)	\$ 6,487
Customer Type					
Federal	\$ 1,851	\$ 3,792	\$ 629	\$ —	\$ 6,272
Commercial	—	—	215	—	215
Intersegment	2	4	96	(102)	—
Sales and service revenues	\$ 1,853	\$ 3,796	\$ 940	\$ (102)	\$ 6,487
Contract Type					
Firm fixed-price	\$ 61	\$ 5	\$ 159	\$ —	\$ 225
Fixed-price incentive	1,487	1,591	1	—	3,079
Cost-type	303	2,196	375	—	2,874
Time and materials	—	—	309	—	309
Intersegment	2	4	96	(102)	—
Sales and service revenues	\$ 1,853	\$ 3,796	\$ 940	\$ (102)	\$ 6,487

Nine Months Ended September 30, 2018

(\$ in millions)	Ingalls	Newport News	Technical Solutions	Intersegment Eliminations	Total
Revenue Type					
Product sales	\$ 1,747	\$ 2,616	\$ 53	\$ —	\$ 4,416
Service revenues	159	823	579	—	1,561
Intersegment	2	5	89	(96)	—
Sales and service revenues	\$ 1,908	\$ 3,444	\$ 721	\$ (96)	\$ 5,977
Customer Type					
Federal	\$ 1,906	\$ 3,439	\$ 447	\$ —	\$ 5,792
Commercial	—	—	184	—	184
State and local government agencies	—	—	1	—	1
Intersegment	2	5	89	(96)	—
Sales and service revenues	\$ 1,908	\$ 3,444	\$ 721	\$ (96)	\$ 5,977
Contract Type					
Firm fixed-price	\$ 73	\$ 6	\$ 114	\$ —	\$ 193
Fixed-price incentive	1,583	1,369	1	—	2,953
Cost-type	250	2,064	275	—	2,589
Time and materials	—	—	242	—	242
Intersegment	2	5	89	(96)	—
Sales and service revenues	\$ 1,908	\$ 3,444	\$ 721	\$ (96)	\$ 5,977

	Three Months Ended September 30	Three Months Ended September 30	Nine Months Ended September 30	Nine Months Ended September 30
(\$ in millions)	2019	2018	2019	2018
Major Programs				
Amphibious assault ships	\$ 349	\$ 356	\$ 971	\$ 971
Surface combatants and coast guard cutters	294	336	875	934
Other	4	2	7	3
Total Ingalls	647	694	1,853	1,908
Aircraft carriers	707	647	2,166	1,888
Submarines	390	369	1,121	1,114
Other	167	163	509	442
Total Newport News	1,264	1,179	3,796	3,444
Government and energy services	284	194	772	589
Oil and gas services	63	51	168	132
Total Technical Solutions	347	245	940	721
Intersegment eliminations	(39)	(35)	(102)	(96)
Sales and service revenues	\$ 2,219	\$ 2,083	\$ 6,487	\$ 5,977

As of September 30, 2019, the Company had \$39.2 billion of remaining performance obligations. The Company expects to recognize approximately 20% of its remaining performance obligations as revenue through 2020, an additional 30% through 2022, and the balance thereafter.

Cumulative Catch-up Adjustments

For the three months ended September 30, 2019, net cumulative catch-up adjustments increased operating income and diluted earnings per share by \$44 million and \$0.86, respectively. For the three months ended September 30, 2018, net cumulative catch-up adjustments increased operating income and diluted earnings per share by \$34 million and \$0.62, respectively. For the nine months ended September 30, 2019, net cumulative catch-up adjustments increased operating income and diluted earnings per share by \$57 million and \$1.09, respectively. For the nine months ended September 30, 2018, net cumulative catch-up adjustments increased operating income and diluted earnings per share by \$99 million and \$1.78, respectively. No individual adjustment was material to the Company's unaudited condensed consolidated statements of operations and comprehensive income for the three and nine months ended September 30, 2019 and 2018.

Contract Balances

Contract balances include accounts receivable, contract assets, and contract liabilities from contracts with customers. Accounts receivable represent an unconditional right to consideration and include amounts billed and currently due from customers. Contract assets primarily relate to the Company's rights to consideration for work completed but not billed as of the reporting date when the right to payment is not just subject to the passage of time. Fixed-price contracts are generally billed to the customer using either progress payments, whereby amounts are billed monthly as costs are incurred or work is completed, or performance based payments, which are based upon the achievement of specific, measurable events or accomplishments defined and valued at contract inception. Cost-type contracts are typically billed to the customer on a monthly or semi-monthly basis. Contract liabilities relate to advance payments, billings in excess of revenues, and deferred revenue amounts.

The Company reports contract balances in a net contract asset or contract liability position on a contract-by-contract basis at the end of each reporting period. The Company's net contract assets increased \$202 million from December 31, 2018, to September 30, 2019, primarily due to an increase in contract assets as a result of revenue on certain U.S. Navy contracts. For the three and nine months ended September 30, 2019, the Company recognized revenue of \$17 million and \$261 million, respectively, related to its contract liabilities as of December 31, 2018. For the nine months ended September 30, 2018, the Company recognized revenue of \$87 million related to its contract liabilities as of December 31, 2017.

9. SEGMENT INFORMATION

The Company is organized into three reportable segments: Ingalls, Newport News, and Technical Solutions, consistent with how management makes operating decisions and assesses performance.

The following table presents segment results for the three and nine months ended September 30, 2019 and 2018:

(\$ in millions)	Three Months Ended September 30		Nine Months Ended September 30	
	2019	2018	2019	2018
Sales and Service Revenues				
Ingalls	\$ 647	\$ 694	\$ 1,853	\$ 1,908
Newport News	1,264	1,179	3,796	3,444
Technical Solutions	347	245	940	721
Intersegment eliminations	(39)	(35)	(102)	(96)
Sales and service revenues	<u>\$ 2,219</u>	<u>\$ 2,083</u>	<u>\$ 6,487</u>	<u>\$ 5,977</u>
Operating Income				
Ingalls	\$ 61	\$ 82	\$ 176	\$ 229
Newport News	109	119	257	261
Technical Solutions	21	16	25	25
Segment operating income	<u>191</u>	<u>217</u>	<u>458</u>	<u>515</u>
Non-segment factors affecting operating income (loss)				
Operating FAS/CAS Adjustment	23	73	94	218
Non-current state income taxes	—	—	(2)	5
Operating income	<u>\$ 214</u>	<u>\$ 290</u>	<u>\$ 550</u>	<u>\$ 738</u>

Operating FAS/CAS Adjustment - The Operating FAS/CAS Adjustment represents the difference between the service cost component of our pension and other postretirement expense determined in accordance with GAAP ("FAS") and our pension and other postretirement expense under CAS.

The following table presents the Company's assets by segment:

(\$ in millions)	September 30 2019	December 31 2018
Assets		
Ingalls	\$ 1,712	\$ 1,448
Newport News	3,945	3,572
Technical Solutions	1,134	734
Corporate	393	629
Total assets	<u>\$ 7,184</u>	<u>\$ 6,383</u>

10. INVENTORIED COSTS, NET

Inventoried costs were comprised of the following:

(\$ in millions)	September 30 2019	December 31 2018
Production costs of contracts in process ¹	\$ 37	\$ 34
Raw material inventory	102	94
Total inventoried costs, net	<u>\$ 139</u>	<u>\$ 128</u>

¹ Includes amounts capitalized pursuant to applicable provisions of the FAR and CAS.

11. GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill

HII performs impairment tests for goodwill as of November 30 of each year and between annual impairment tests if an event occurs or circumstances change that would more likely than not reduce the fair values of the Company's reporting units below their carrying values.

Accumulated goodwill impairment losses as of each of September 30, 2019, and December 31, 2018, were \$2,877 million. The accumulated goodwill impairment losses for Ingalls as of each of September 30, 2019, and December 31, 2018, were \$1,568 million. The accumulated goodwill impairment losses for Newport News as of each of September 30, 2019, and December 31, 2018, were \$1,187 million. The accumulated goodwill impairment losses for Technical Solutions as of each of September 30, 2019, and December 31, 2018, were \$122 million.

For the nine months ended September 30, 2019, the carrying amounts of goodwill changed as follows:

(\$ in millions)	Ingalls	Newport News	Technical Solutions	Total
Balance as of December 31, 2018	175	721	367	1,263
Acquisitions	—	—	133	133
Adjustments	—	—	6	6
Balance as of September 30, 2019	\$ 175	\$ 721	\$ 506	\$ 1,402

Other Intangible Assets

The Company's purchased intangible assets are amortized on a straight-line basis or a method based on the pattern of benefits over their estimated useful lives. Net intangible assets consist principally of amounts pertaining to nuclear-powered aircraft carrier and submarine program intangible assets, with an aggregate weighted-average useful life of 40 years based on the long life cycle of the related programs. Aggregate amortization expense was \$12 million and \$10 million for the three months ended September 30, 2019 and 2018, respectively. Aggregate amortization expense was \$35 million and \$28 million for the nine months ended September 30, 2019 and 2018, respectively.

In connection with the Fulcrum purchase in 2019, the Company recorded \$49 million of intangible assets pertaining to existing contract backlog and customer relationships, to be amortized using the pattern of benefits method over a weighted-average life of seven years. In connection with the G2 purchase in 2018, the Company recorded \$20 million of intangible assets pertaining to existing contract backlog and customer relationships, to be amortized using the pattern of benefits method over a weighted-average life of seven years.

The Company expects amortization expense for purchased intangible assets of approximately \$47 million in 2019, \$44 million in 2020, \$40 million in 2021, \$37 million in 2022, and \$27 million in 2023.

12. INCOME TAXES

The Company's earnings are primarily domestic, and its effective income tax rates on earnings from operations for the three months ended September 30, 2019 and 2018, were 22.2% and 22.4%, respectively. For the nine months ended September 30, 2019 and 2018, the Company's effective income tax rates on earnings from operations were 21.7% and 17.0%, respectively. The higher effective income tax rate for the nine months ended September 30, 2019, was primarily attributable to a claim for higher research and development tax credits for the post-spin-off 2011 through 2015 tax years recorded in 2018.

For the three months ended September 30, 2019, the Company's effective income tax rate differed from the federal statutory rate primarily as a result of a non-recurring increase in tax expense for the true-up of estimated income taxes to the actual filed return. For the nine months ended September 30, 2019, the Company's effective income tax rate differed from the federal statutory rate primarily as a result of an unfavorable adjustment to claims for research and development tax credits for prior tax years and a non-recurring increase in tax expense for the true-up of estimated income taxes to the actual filed return, partially offset by income tax benefits resulting from stock award settlement activity. For the three and nine months ended September 30, 2018, the Company's effective

income tax rate differed from the federal statutory rate primarily as a result of a claim for higher research and development tax credits for the post-spin-off 2011 through 2015 tax years.

The Company's unrecognized tax benefits changed by less than \$1 million during the three and nine months ended September 30, 2019. As of September 30, 2019, the estimated amounts of the Company's unrecognized tax benefits, excluding interest and penalties, were liabilities of \$24 million. Assuming a sustainment of these tax positions, the reversal of the \$24 million accrual would favorably affect the Company's effective federal income tax rate in future periods.

The Company recognizes interest and penalties related to unrecognized tax benefits as income tax expense. For the three and nine months ended September 30, 2019, interest resulting from the unrecognized tax benefits noted above increased income tax expense less than \$1 million. Non-current state income taxes include deferred state income taxes, which reflect the change in deferred state tax assets and liabilities, and the tax expense or benefit associated with changes in unrecognized tax benefits in the relevant period. These amounts are recorded within operating income. Current period state income tax expense is charged to contract costs and included in cost of sales and service revenues in segment operating income.

13. DEBT

Long-term debt consisted of the following:

(\$ in millions)	September 30 2019	December 31 2018
Senior notes due November 15, 2025, 5.000%	600	600
Senior notes due December 1, 2027, 3.483%	600	600
Mississippi economic development revenue bonds due May 1, 2024, 7.81%	84	84
Gulf opportunity zone industrial development revenue bonds due December 1, 2028, 4.55%	21	21
Revolving credit facility borrowings	264	—
Less unamortized debt issuance costs	(20)	(22)
Total long-term debt	\$ 1,549	\$ 1,283

Credit Facility - The Company's credit facility with third-party lenders (the "Credit Facility") includes a revolving credit facility of \$1,250 million, which may be drawn upon during a period of five years from November 22, 2017. The revolving credit facility includes a letter of credit subfacility of \$500 million.

The Credit Facility contains customary affirmative and negative covenants, as well as a financial covenant based on a maximum total leverage ratio. Each of the Company's existing and future material wholly owned domestic subsidiaries, except those that are specifically designated as unrestricted subsidiaries, are and will be guarantors under the Credit Facility.

As of September 30, 2019, the Company had \$264 million of outstanding borrowings, \$22 million in issued but undrawn letters of credit, and \$964 million unutilized under the Credit Facility. The Company had unamortized debt issuance costs associated with its credit facilities of \$7 million and \$8 million as of September 30, 2019, and December 31, 2018, respectively. The Company had unamortized debt issuance costs associated with its senior notes of \$13 million and \$14 million as of September 30, 2019, and December 31, 2018, respectively.

In October 2019, the Company established an unsecured commercial paper note program, under which the Company may issue up to \$1 billion of unsecured commercial paper notes.

The Company's debt arrangements contain customary affirmative and negative covenants. The Company was in compliance with all debt covenants during the nine months ended September 30, 2019.

The estimated fair values of the Company's total long-term debt as of September 30, 2019, and December 31, 2018, were \$1,642 million and \$1,292 million, respectively. The fair values of the Company's long-term debt were calculated based on recent trades of the Company's debt instruments in inactive markets, which fall within Level 2 under the fair value hierarchy.

14. INVESTIGATIONS, CLAIMS, AND LITIGATION

The Company is involved in legal proceedings before various courts and administrative agencies, and is periodically subject to government examinations, inquiries and investigations. Pursuant to FASB Accounting Standards Codification 450 *Contingencies*, the Company has accrued for losses associated with investigations, claims, and litigation when, and to the extent that, loss amounts related to the investigations, claims, and litigation are probable and can be reasonably estimated. The actual losses that might be incurred to resolve such investigations, claims, and litigation may be higher or lower than the amounts accrued. For matters where a material loss is probable or reasonably possible and the amount of loss cannot be reasonably estimated, but the Company is able to reasonably estimate a range of possible losses, the Company will disclose such estimated range in these notes. This estimated range is based on information currently available to the Company and involves elements of judgment and significant uncertainties. Any estimated range of possible loss does not represent the Company's maximum possible loss exposure. For matters as to which the Company is not able to reasonably estimate a possible loss or range of loss, the Company will indicate the reasons why it is unable to estimate the possible loss or range of loss. For matters not specifically described in these notes, the Company does not believe, based on information currently available to it, that it is reasonably possible that the liabilities, if any, arising from such investigations, claims, and litigation will have a material effect on its consolidated financial position, results of operations, or cash flows. The Company has, in certain cases, provided disclosure regarding certain matters for which the Company believes at this time that the likelihood of material loss is remote.

False Claims Act Complaint - In 2016, the Company was made aware that it is a defendant in a *qui tam* False Claims Act lawsuit pending in the U.S. District Court for the Middle District of Florida related to the Company's purchases of allegedly non-conforming parts from a supplier for use in connection with U.S. Government contracts. In August 2019, the Department of Justice ("DoJ") declined to intervene in the lawsuit, and the lawsuit was unsealed. Depending on the outcome of the lawsuit, the Company could be subject to civil penalties, damages, and/or suspension or debarment from future U.S. Government contracts, which could have a material adverse effect on its consolidated financial position, results of operations, or cash flows. The Company has not yet been served with the lawsuit and therefore has not had an opportunity to respond to the complaint or engage in any discovery related to the issues set forth in the complaint. As a result, the Company currently is unable to estimate an amount or range of reasonably possible loss or to express an opinion regarding the ultimate outcome.

In September 2019, the Company became aware that it is a defendant in a *qui tam* False Claims Act lawsuit pending in the U.S. District Court for the Middle District of Florida related to allegations about the Company's application of a material to the exterior surface of *Virginia* class (SSN 774) submarines. The DoJ declined to intervene in the lawsuit, and the lawsuit was unsealed. Depending on the outcome of the lawsuit, the Company could be subject to civil penalties, damages, and/or suspension or debarment from future U.S. Government contracts, which could have a material adverse effect on its consolidated financial position, results of operations, or cash flows. The Company has not yet been served with the lawsuit and therefore has not had an opportunity to respond to the complaint or engage in any discovery related to the issues set forth in the complaint. As a result, the Company currently is unable to estimate an amount or range of reasonably possible loss or to express an opinion regarding the ultimate outcome.

U.S. Government Investigations and Claims - Departments and agencies of the U.S. Government have the authority to investigate various transactions and operations of the Company, and the results of such investigations may lead to administrative, civil, or criminal proceedings, the ultimate outcome of which could be fines, penalties, repayments or compensatory, treble, or other damages. U.S. Government regulations provide that certain findings against a contractor may also lead to suspension or debarment from future U.S. Government contracts or the loss of export privileges. Any suspension or debarment would have a material effect on the Company because of its reliance on government contracts.

Asbestos Related Claims - HII and its predecessors-in-interest are defendants in a longstanding series of cases that have been and continue to be filed in various jurisdictions around the country, wherein former and current employees and various third parties allege exposure to asbestos containing materials while on or associated with HII premises or while working on vessels constructed or repaired by HII. The cases allege various injuries, including those associated with pleural plaque disease, asbestosis, cancer, mesothelioma, and other alleged asbestos related conditions. In some cases, several of HII's former executive officers are also named as defendants. In some instances, partial or full insurance coverage is available to the Company for its liability and that of its former executive officers. The costs to resolve cases during the nine months ended September 30, 2019 and 2018, were

immaterial individually and in the aggregate. The Company's estimate of asbestos-related liabilities is subject to uncertainty because liabilities are influenced by numerous variables that are inherently difficult to predict. Key variables include the number and type of new claims, the litigation process from jurisdiction to jurisdiction and from case to case, reforms made by state and federal courts, and the passage of state or federal tort reform legislation. Although the Company believes the ultimate resolution of current cases will not have a material effect on its consolidated financial position, results of operations, or cash flows, it cannot predict what new or revised claims or litigation might be asserted or what information might come to light and can, therefore, give no assurances regarding the ultimate outcome of asbestos related litigation.

Other Litigation - In March 2019, a new dry dock being transported for delivery to Ingalls by a heavy lift ship struck an Ingalls work barge, which in turn was pushed into *Delbert D. Black* (DDG 119) causing damage to *Delbert D. Black* (DDG 119), the work barge, and the new dry dock. At the time of the incident, responsibility for the new dry dock remained with the builder and the transport company. Repair work on *Delbert D. Black* (DDG 119) is in process at U.S. Navy direction. The Company is working with the U.S. Navy to ascertain whether third parties will pay for the repairs to *Delbert D. Black* (DDG 119) or whether the repairs will be paid under the builder's risk insurance included in the *Delbert D. Black* (DDG 119) contract. Claims have been tendered to the Company's insurers, and HII is continuing to receive claim proceeds. In April 2019, the Company filed suit in the U.S. District Court for the Southern District of Mississippi seeking, among other relief, damages from negligent third parties. Based on information currently available, management believes it will collect sufficient funds from one or more third parties to compensate for the resulting direct and consequential damages, but failure to collect sufficient funds or the length of time required to collect such funds could result in a material effect on the Company's financial position, results of operations, or cash flows.

The Company and its predecessor-in-interest have been in litigation with the Bolivarian Republic of Venezuela (the "Republic") since 2002 over a contract for the repair, refurbishment, and modernization at Ingalls of two foreign-built frigates. The case proceeded towards arbitration, then appeared to settle favorably, but the settlement was overturned in court and the matter returned to litigation. In March 2014, the Company filed an arbitral statement of claim asserting breaches of the contract. In July 2014, the Republic filed a statement of defense in the arbitration denying all the Company's allegations and a counterclaim alleging late redelivery of the frigates, unfinished work, and breach of warranty. In February 2018, the arbitral tribunal awarded the Company approximately \$151 million on its claims and awarded the Republic approximately \$22 million on its counterclaims. The Company is seeking to enforce and execute upon the award in multiple jurisdictions. No assurances can be provided regarding the ultimate resolution of this matter.

The Company is party to various other claims, legal proceedings and investigations that arise in the ordinary course of business, including U.S. Government investigations that could result in administrative, civil, or criminal proceedings involving the Company. The Company is a contractor with the U.S. Government, and such proceedings can therefore include False Claims Act allegations against the Company. Although the Company believes that the resolution of these other claims, legal proceedings and investigations will not have a material effect on its consolidated financial position, results of operations, or cash flows, the Company cannot predict what new or revised claims or litigation might be asserted or what information might come to light and can, therefore, give no assurances regarding the ultimate outcome of these matters.

15. LEASES

The Company leases certain land, warehouses, office space, and production, office, and technology equipment, among other items. Most equipment is leased on a monthly basis. Many land, warehouse, and office space leases include renewal terms that can extend the lease term. The exercise of lease renewal options is at our sole discretion. The depreciable life of assets and leasehold improvements are generally limited by the expected lease term. Our lease agreements do not generally contain material residual value guarantees, material restrictive covenants, or purchase options. Our lease portfolio consists primarily of operating leases. Amounts prior to January 1, 2019, are reported under Topic 840, and amounts after January 1, 2019, are reported under Topic 842 in accordance with ASU 2016-02.

Lease costs and related information were as follows:

	Three Months Ended September 30	Nine Months Ended September 30
(\$ in millions)	2019	2019
Operating lease costs	\$ 12	\$ 35
Short-term operating lease costs	\$ 9	\$ 21
Variable operating lease costs	\$ 2	\$ 5
Operating cash flows from operating leases	\$ (12)	\$ (34)
Right-of-use assets obtained in exchange for new operating lease liabilities	\$ 4	\$ 21
Weighted-average remaining lease term (years) - operating leases	11 years	11 years
Weighted-average discount rate - operating leases	4.5%	4.5%

The undiscounted future non-cancellable lease payments under our operating leases were as follows:

Year:	September 30 2019	December 31 2018
2019	\$ 11	\$ 41
2020	42	36
2021	36	30
2022	29	20
2023	22	13
Thereafter	127	56
Total lease payments	267	196
Less: imputed interest	59	—
Present value of lease liabilities	\$ 208	\$ —

Lease liabilities included in the Company's consolidated balance sheet as of September 30, 2019, were as follows:

(\$ in millions)	
Short-term operating lease liabilities	\$ 36
Long-term operating lease liabilities	172
Total operating lease liabilities	\$ 208

16. COMMITMENTS AND CONTINGENCIES

Contract Performance Contingencies - Contract profit margins may include estimates of revenues for matters on which the customer and the Company have not reached agreement, such as settlements in the process of negotiation, contract changes, claims, and requests for equitable adjustment for unanticipated contract costs. These estimates are based upon management's best assessment of the underlying causal events and circumstances and are included in contract profit margins to the extent of expected recovery based upon contractual entitlements and the probability of successful negotiation with the customer. As of September 30, 2019, amounts recognized in connection with claims and requests for equitable adjustment were not material individually or in aggregate.

Guarantees of Performance Obligations - From time to time in the ordinary course of business, HII may enter into joint ventures, teaming, and other business arrangements to support the Company's products and services. The Company attempts to limit its exposure under these arrangements to its investment or the extent of obligations under the applicable contract. In some cases, however, HII may be required to guarantee performance of the arrangement's obligations and, in such cases, generally obtains cross-indemnification from the other members of the arrangement.

In the ordinary course of business, the Company may guarantee obligations of its subsidiaries under certain contracts. Generally, the Company is liable under such an arrangement only if its subsidiary is unable to perform its

obligations. Historically, the Company has not incurred any substantial liabilities resulting from these guarantees. As of September 30, 2019, the Company was not aware of any existing event of default that would require it to satisfy any of these guarantees.

Environmental Matters - The estimated cost to complete environmental remediation has been accrued when it is probable that the Company will incur such costs in the future to address environmental conditions at currently or formerly owned or leased operating facilities, or at sites where it has been named a Potentially Responsible Party ("PRP") by the Environmental Protection Agency or similarly designated by another environmental agency, and the related costs can be estimated by management. These accruals do not include any litigation costs related to environmental matters, nor do they include amounts recorded as asset retirement obligations. To assess the potential impact on the Company's consolidated financial statements, management estimates the range of reasonably possible remediation costs that could be incurred by the Company, taking into account currently available facts on each site, as well as the current state of technology and prior experience remediating contaminated sites. These estimates are reviewed periodically and adjusted to reflect changes in facts and technical and legal circumstances. Management estimated that as of September 30, 2019, the probable estimable future cost for environmental remediation was immaterial. Factors that could result in changes to the Company's estimates include: modification of planned remedial actions, increases or decreases in the estimated time required to remediate, changes to the determination of legally responsible parties, discovery of more extensive contamination than anticipated, changes in laws and regulations affecting remediation requirements, and improvements in remediation technology. Should other PRPs not pay their allocable share of remediation costs, the Company may incur costs exceeding those already estimated and accrued. In addition, there are certain potential remediation sites where the costs of remediation cannot be reasonably estimated. Although management cannot predict whether new information gained as remediation progresses will materially affect the estimated liability accrued, management does not believe that future remediation expenditures will have a material effect on the Company's consolidated financial position, results of operations, or cash flows.

Financial Arrangements - In the ordinary course of business, HII uses standby letters of credit issued by commercial banks and surety bonds issued by insurance companies primarily to support the Company's self-insured workers' compensation plans. As of September 30, 2019, the Company had \$22 million in issued but undrawn standby letters of credit, as indicated in Note 13: Debt, and \$273 million of surety bonds outstanding.

U.S. Government Claims - From time to time, the U.S. Government communicates to the Company potential claims, disallowed costs, and penalties concerning prior costs incurred by the Company with which the U.S. Government disagrees. When such preliminary findings are presented, the Company and U.S. Government representatives engage in discussions, from which HII evaluates the merits of the claims and assesses the amounts being questioned. Although the Company believes that the resolution of any of these matters will not have a material effect on its consolidated financial position, results of operations, or cash flows, it cannot predict the ultimate outcome of these matters.

Collective Bargaining Agreements - Of the Company's approximately 41,000 employees, approximately 50% are covered by a total of nine collective bargaining agreements and two site stabilization agreements. Newport News has four collective bargaining agreements covering represented employees, which expire in December 2019, November 2020, November 2021, and December 2022. The collective bargaining agreement that expires in November 2021 covers approximately 50% of Newport News employees. Newport News craft workers employed at the Kesselring Site near Saratoga Springs, New York are represented under an indefinite Department of Energy ("DoE") site agreement. Ingalls has five collective bargaining agreements covering represented employees, all of which expire in March 2022. Approximately 50 Technical Solutions employees at various locations are represented by unions and perform work under collective bargaining agreements. The Company believes its relationship with its employees is satisfactory.

Collective bargaining agreements generally expire after three years to five years and are subject to renegotiation at that time. The Company does not expect the results of these negotiations, either individually or in the aggregate, to have a material effect on the Company's consolidated results of operations.

17. EMPLOYEE PENSION AND OTHER POSTRETIREMENT BENEFITS

The Company provides eligible employees defined benefit pension plans, postretirement benefit plans, and defined contribution pension plans.

The costs of the Company's defined benefit pension plans and other postretirement benefit plans for the three and nine months ended September 30, 2019 and 2018, were as follows:

(\$ in millions)	Three Months Ended September 30				Nine Months Ended September 30			
	Pension Benefits		Other Benefits		Pension Benefits		Other Benefits	
	2019	2018	2019	2018	2019	2018	2019	2018
Components of Net Periodic Benefit Cost								
Service cost	\$ 36	\$ 39	\$ 2	\$ 2	\$ 108	\$ 118	\$ 5	\$ 6
Interest cost	69	63	5	5	208	190	15	15
Expected return on plan assets	(102)	(107)	—	—	(305)	(322)	—	—
Amortization of prior service cost (credit)	4	6	(5)	(5)	13	18	(16)	(16)
Amortization of net actuarial loss (gain)	29	20	(3)	(1)	85	61	(8)	(2)
Net periodic benefit cost	<u>\$ 36</u>	<u>\$ 21</u>	<u>\$ (1)</u>	<u>\$ 1</u>	<u>\$ 109</u>	<u>\$ 65</u>	<u>\$ (4)</u>	<u>\$ 3</u>

The Company made the following contributions to its defined benefit pension plans and other postretirement benefit plans for the nine months ended September 30, 2019 and 2018:

(\$ in millions)	Nine Months Ended September 30	
	2019	2018
Pension plans		
Qualified minimum	\$ —	\$ —
Discretionary		
Qualified	21	508
Non-qualified	5	6
Other benefit plans	23	23
Total contributions	<u>\$ 49</u>	<u>\$ 537</u>

As of September 30, 2019, the Company anticipates no further significant cash contributions to its qualified defined benefit pension plans in 2019.

18. STOCK COMPENSATION PLANS

During the nine months ended September 30, 2019 and 2018, the Company issued new stock awards as follows:

Restricted Performance Stock Rights - For the nine months ended September 30, 2019, the Company granted approximately 0.1 million RPSRs at a weighted average share price of \$210.24. These rights are subject to cliff vesting on December 31, 2021. For the nine months ended September 30, 2018, the Company granted approximately 0.1 million RPSRs at a weighted average share price of \$261.89. These rights are subject to cliff vesting on December 31, 2020. All of the RPSRs are subject to the achievement of performance-based targets at the end of the respective vesting periods and will ultimately vest between 0% and 200% of grant date value.

For the nine months ended September 30, 2019 and 2018, 0.3 million and 0.2 million stock awards vested, respectively, of which approximately 0.1 million for each year were transferred to the Company from employees in satisfaction of minimum tax withholding obligations.

The following table summarizes the status of the Company's outstanding stock awards as of September 30, 2019:

	Stock Awards (in thousands)	Weighted-Average Grant Date Fair Value	Weighted-Average Remaining Contractual Term (in years)
Total stock awards	371	\$ 201.91	1.1

Compensation Expense

The Company recorded stock-based compensation for the value of awards granted to Company employees and non-employee members of the board of directors for the three months ended September 30, 2019 and 2018, of \$7 million and \$11 million, respectively. The Company recorded stock-based compensation for the value of awards granted to Company employees and non-employee members of the board of directors for the nine months ended September 30, 2019 and 2018, of \$19 million and \$27 million, respectively.

The Company recorded tax benefits related to stock awards of \$1 million and \$3 million for the three months ended September 30, 2019 and 2018, respectively. The Company recorded tax benefits related to stock awards of \$3 million and \$6 million for the nine months ended September 30, 2019 and 2018, respectively. The Company recognized tax benefits associated with the issuance of stock in settlement of stock awards for the three months ended September 30, 2019 and 2018, of less than \$1 million. The Company recognized tax benefits associated with the issuance of stock in settlement of stock awards for the nine months ended September 30, 2019 and 2018, of \$5 million and \$7 million, respectively.

Unrecognized Compensation Expense

As of September 30, 2019, the Company had less than \$1 million of unrecognized compensation expense associated with Restricted Stock Rights granted in 2018, which will be recognized over a weighted average period of 1.4 years, and \$33 million of unrecognized compensation expense associated with RPSRs granted in 2019, 2018, and 2017, which will be recognized over a weighted average period of 1.4 years.

19. SUBSIDIARY GUARANTORS

As described in Note 13: Debt, the Company issued senior notes through the consolidating parent company, HII. Performance of the Company's obligations under its senior notes outstanding as of September 30, 2019, and December 31, 2018, including any repurchase obligations resulting from a change of control, is fully and unconditionally guaranteed, jointly and severally, on an unsecured basis, by each of HII's existing and future material domestic subsidiaries ("Subsidiary Guarantors"). The Subsidiary Guarantors are 100% owned by HII. Under SEC Regulation S-X Rule 3-10, each HII subsidiary that did not provide a guarantee ("Non-Guarantors") is minor and HII, as the parent company issuer, did not have independent assets or operations. There are no significant restrictions on the ability of the parent company and the Subsidiary Guarantors to obtain funds from their respective subsidiaries by dividend or loan, except those imposed by applicable law.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

OVERVIEW

Our Business

Huntington Ingalls Industries, Inc. ("HII", "we", "us", or "our") is America's largest military shipbuilding company and a provider of professional services to partners in government and industry. For more than a century, our Ingalls segment in Mississippi and Newport News segment in Virginia have built more ships in more ship classes than any other U.S. naval shipbuilder. We also provide a range of services to the governmental, energy, and oil and gas markets through our Technical Solutions segment. Headquartered in Newport News, Virginia, HII employs approximately 41,000 people domestically and internationally.

We conduct most of our business with the U.S. Government, primarily the DoD. As prime contractor, principal subcontractor, team member, or partner, we participate in many high-priority U.S. defense technology programs.

Ingalls includes our non-nuclear ship design, construction, repair, and maintenance businesses. Newport News includes all of our nuclear ship design, construction, overhaul, refueling, and repair and maintenance businesses. Our Technical Solutions segment provides a wide range of professional services, including fleet support, MDIS, nuclear and environmental, and oil and gas services.

The following discussion should be read along with the unaudited condensed consolidated financial statements included in this Quarterly Report on Form 10-Q, as well as our Annual Report on Form 10-K for the year ended December 31, 2018.

Business Environment

In August 2011, the Budget Control Act (the "BCA") established limits on U.S. Government discretionary spending, including a reduction of defense spending by approximately \$487 billion for fiscal years 2012 through 2021. The BCA also provided that the defense budget would face "sequestration" cuts of up to an additional \$500 billion during that same period, to the extent that discretionary spending limits are exceeded, and \$500 billion for non-defense discretionary spending, including the U.S. Coast Guard.

The Bi-Partisan Budget Act ("BBA") of 2018 provided sequestration relief for fiscal years 2018 and 2019 and raised the budget topline for defense and non-defense discretionary spending. Subsequently, the BBA of 2019 provided sequestration relief for fiscal years 2020 and 2021, and once again raised the topline for defense and non-defense discretionary spending. Even though the 2019 BBA provides budgetary relief through 2021, the final year of sequestration, long-term uncertainty remains with respect to overall levels of defense spending across the future years' defense plan, and it is likely that U.S. Government discretionary spending levels will continue to be subject to significant pressure.

The President's budget request for fiscal year 2020 was released on March 11, 2019, and is under consideration by Congress. While the budget request reflects continued investment in submarines, destroyers, aircraft carriers, amphibious warships, and autonomous platforms, the budget request proposed canceling the refueling and complex overhaul of USS *Harry S. Truman* (CVN 75). The Administration subsequently announced in April 2019 that USS *Harry S. Truman* (CVN 75) would be refueled.

While the 2019 BBA established new funding levels for defense and non-defense discretionary spending for fiscal year 2020, respective appropriations measures must still be passed by Congress and enacted by the President. We cannot predict the outcome of the fiscal year 2020 budget process. We also cannot predict the impact reprioritization of readiness and modernization investment may have on funding for our individual programs. Long-term funding for certain programs in which we participate may be reduced, delayed, or canceled. In addition, spending cuts and/or reprioritization of defense investment could adversely affect the viability of our suppliers, subcontractors, and employee base. Our contracts or subcontracts under programs in which we participate may be terminated or adjusted by the U.S. Government or the prime contractor as a result of lack of government funding or reductions or delays in government funding. Significant reductions in the number of ships procured by the U.S. Navy or significant delays in funding our ship programs would have a material effect on our financial position, results of operations, or cash flows.

The budget environment remains a significant long-term risk. Considerable uncertainty exists regarding how future budget and program decisions will develop and what challenges budget changes will present for the defense industry. We believe continued budget pressures will have serious implications for defense discretionary spending, the defense industrial base, including us, and the customers, employees, suppliers, subcontractors, investors, and communities that rely on companies in the defense industrial base. Although it is difficult to determine specific impacts, we expect that over the longer term, the budget environment may result in fewer contract awards and lower revenues, profits, and cash flows from our U.S. Government contracts. It is likely that budget and program decisions made in this environment will have long-term impacts on us and the entire defense industry.

Critical Accounting Policies, Estimates, and Judgments

As discussed in our Annual Report on Form 10-K for the year ended December 31, 2018, we consider our policies relating to the following matters to be critical accounting policies:

- Revenue recognition;

- Purchase accounting, goodwill, and intangible assets;
- Litigation, commitments, and contingencies;
- Retirement related benefit plans; and
- Workers' compensation.

As of September 30, 2019, there had been no material changes to the foregoing critical accounting policies, estimates, and judgments since December 31, 2018.

Contracts

We generate most of our revenues from long-term U.S. Government contracts for design, production, and support activities. Government contracts typically include the following cost elements: direct material, labor and subcontracting costs, and certain indirect costs, including allowable general and administrative expenses. Unless otherwise specified in a contract, costs billed to contracts with the U.S. Government are treated as allowable and allocable costs under the Federal Acquisition Regulation ("FAR") and the U.S. Cost Accounting Standards ("CAS") regulations. Examples of costs incurred by us that are not allowable under the FAR and CAS regulations include certain legal costs, lobbying costs, charitable donations, interest expense, and advertising costs.

We monitor our policies and procedures with respect to our contracts on a regular basis to ensure consistent application under similar terms and conditions, as well as compliance with all applicable government regulations. In addition, the Defense Contract Audit Agency routinely audits the costs we incur that are allocated to contracts with the U.S. Government.

Our contracts typically fall into one of four categories: firm fixed-price, fixed-price incentive, cost-type, and time and materials. See Note 8: Revenue.

- *Firm Fixed-Price Contracts* - A firm fixed-price contract is a contract in which the specified scope of work is agreed to for a price that is predetermined by bid or negotiation and not generally subject to adjustment regardless of costs incurred by the contractor.
- *Fixed-Price Incentive Contracts* - Fixed-price incentive contracts provide for reimbursement of the contractor's allowable costs, but are subject to a cost-share limit that affects profitability. Fixed-price incentive contracts effectively become firm fixed-price contracts once the cost-share limit is reached.
- *Cost-Type Contracts* - Cost-type contracts provide for reimbursement of the contractor's allowable costs plus a fee that represents profit. Cost-type contracts generally require that the contractor use its reasonable efforts to accomplish the scope of the work within some specified time and some stated dollar limitation.
- *Time and Materials* - Time and materials contracts specify a fixed hourly billing rate for each direct labor hour expended and reimbursement for allowable material costs and expenses.

Contract Fees - Negotiated contract fee structures include: fixed fee amounts, cost sharing arrangements to reward or penalize contractors for under or over cost target performance, respectively, positive award fees, and negative penalty arrangements. Profit margins may vary materially depending on the negotiated contract fee arrangements, percentage-of-completion of the contract, the achievement of performance objectives, and the stage of performance at which the right to receive fees, particularly under incentive and award fee contracts, is finally determined.

Award Fees - Certain contracts contain award fees based on performance criteria such as cost, schedule, quality, and technical performance. Award fees are determined and earned based on an evaluation by the customer of our performance against such negotiated criteria. We consider award fees to be variable consideration and generally include these fees in the transaction price using a most likely amount approach. Award fees are limited to the extent of funding allotted by the customer and available for performance and those amounts for which a significant reversal of revenue is not probable.

Program Descriptions

For convenience, a brief description of certain programs discussed in this Quarterly Report on Form 10-Q is included in the "Glossary of Programs" in this section.

CONSOLIDATED OPERATING RESULTS

The following table presents selected financial highlights:

(\$ in millions)	Three Months Ended		2019 over 2018		Nine Months Ended		2019 over 2018	
	September 30				September 30			
	2019	2018	Dollars	Percent	2019	2018	Dollars	Percent
Sales and service revenues	\$ 2,219	\$ 2,083	\$ 136	7 %	\$ 6,487	\$ 5,977	\$ 510	9 %
Cost of product sales and service revenues	1,802	1,593	209	13 %	5,388	4,656	732	16 %
Income from operating investments, net	6	8	(2)	(25)%	15	12	3	25 %
Other income and gains	—	—	—	— %	—	14	(14)	(100)%
General and administrative expenses	209	208	1	— %	564	609	(45)	(7)%
Operating income	214	290	(76)	(26)%	550	738	(188)	(25)%
Other income (expense)								
Interest expense	(18)	(14)	(4)	(29)%	(52)	(44)	(8)	(18)%
Non-operating retirement benefit	3	19	(16)	(84)%	8	56	(48)	(86)%
Other, net	(1)	—	(1)	— %	5	2	3	150 %
Federal and foreign income taxes	44	66	(22)	(33)%	111	128	(17)	(13)%
Net earnings	\$ 154	\$ 229	\$ (75)	(33)%	\$ 400	\$ 624	\$ (224)	(36)%

Operating Performance Assessment and Reporting

We manage and assess the performance of our business based on our performance on individual contracts and programs using the financial measures referred to below, with consideration given to the Critical Accounting Policies, Estimates, and Judgments referred to in this section. Our portfolio of long-term contracts is largely flexibly-priced. Therefore, sales tend to fluctuate in concert with costs across our large portfolio of active contracts, with operating income being a critical measure of operating performance. Under FAR rules that govern our business with the U.S. Government, most types of costs are allowable, and we do not focus on individual cost groupings, such as cost of sales or general and administrative expenses, as much as we do on total contract costs, which are a key factor in determining contract operating income. As a result, in evaluating our operating performance, we look primarily at changes in sales and service revenues, as well as operating income, including the effects of significant changes in operating income as a result of changes in contract estimates and the use of the cumulative catch-up method of accounting in accordance with GAAP. This approach is consistent with the long-term life cycle of our contracts, as management assesses the bidding of each contract by focusing on net sales and operating profit and monitors performance in a similar manner through contract completion. Consequently, our discussion of business segment performance focuses on net sales and operating profit, consistent with our approach for managing our business.

Cost of sales for both product sales and service revenues consists of materials, labor, and subcontracting costs, as well as an allocation of indirect costs for overhead. We manage the type and amount of costs at the contract level, which is the basis for estimating our total costs at completion of our contracts. Unusual fluctuations in operating performance driven by changes in a specific cost element across multiple contracts are described in our analysis.

Sales and Service Revenues

Sales and service revenues were comprised as follows:

(\$ in millions)	Three Months Ended				Nine Months Ended			
	September 30		2019 over 2018		September 30		2019 over 2018	
	2019	2018	Dollars	Percent	2019	2018	Dollars	Percent
Product sales	\$ 1,545	\$ 1,547	\$ (2)	— %	\$ 4,555	\$ 4,416	\$ 139	3%
Service revenues	674	536	138	26 %	1,932	1,561	371	24%
Sales and service revenues	\$ 2,219	\$ 2,083	\$ 136	7 %	\$ 6,487	\$ 5,977	\$ 510	9%

Product sales for the three months ended September 30, 2019, decreased \$2 million, compared with the same period in 2018. Product sales for the nine months ended September 30, 2019, increased \$139 million, or 3%, compared with the same period in 2018. Ingalls product sales decreased \$52 million for the three months ended September 30, 2019, primarily as a result of lower volumes in the *Legend* class NSC program and amphibious assault ships, partially offset by higher volume in surface combatants. Ingalls product sales decreased \$69 million for the nine months ended September 30, 2019, primarily as a result of lower volumes in the *Legend* class NSC program, amphibious assault ships, and surface combatants. Newport News product sales increased \$61 million and \$226 million for the three and nine months ended September 30, 2019, respectively, primarily as a result of higher volumes in aircraft carriers and submarines. Technical Solutions product sales decreased \$11 million and \$18 million for the three and nine months ended September 30, 2019, respectively, primarily as a result of lower volumes on nuclear and environmental products.

Service revenues for the three months ended September 30, 2019, increased \$138 million, or 26%, compared with the same period in 2018. Service revenues for the nine months ended September 30, 2019, increased \$371 million, or 24%, compared with the same period in 2018. Ingalls service revenues increased \$6 million and \$14 million for the three and nine months ended September 30, 2019, respectively, as a result of higher volumes in amphibious assault ship services, partially offset by lower volume in surface combatant services. Newport News service revenues increased \$24 million for the three months ended September 30, 2019, primarily as a result of higher volumes in aircraft carrier, submarine, and naval nuclear support services. Newport News service revenues increased \$127 million for the nine months ended September 30, 2019, primarily as a result of higher volumes in aircraft carrier and naval nuclear support services, partially offset by lower volume in submarine services. Technical Solutions service revenues increased \$108 million and \$230 million for the three and nine months ended September 30, 2019, respectively, primarily as a result of the addition of Fulcrum and G2, as well as higher volumes in fleet support and oil and gas services.

Cost of Sales and Service Revenues

Cost of product sales, cost of service revenues, income from operating investments, net, and general and administrative expenses were as follows:

(\$ in millions)	Three Months Ended				Nine Months Ended			
	September 30		2019 over 2018		September 30		2019 over 2018	
	2019	2018	Dollars	Percent	2019	2018	Dollars	Percent
Cost of product sales	\$ 1,246	\$ 1,159	\$ 87	8 %	\$ 3,754	\$ 3,369	\$ 385	11 %
% of product sales	80.6%	74.9%			82.4%	76.3%		
Cost of service revenues	556	434	122	28 %	1,634	1,287	347	27 %
% of service revenues	82.5%	81.0%			84.6%	82.4%		
Income from operating investments, net	6	8	(2)	(25)%	15	12	3	25 %
Other income and gains	—	—	—	— %	—	14	(14)	(100)%
General and administrative expenses	209	208	1	— %	564	609	(45)	(7)%
% of sales and service revenues	9.4%	10.0%			8.7%	10.2%		
Cost of sales and service revenues	<u>\$ 2,005</u>	<u>\$ 1,793</u>	<u>\$ 212</u>	12 %	<u>\$ 5,937</u>	<u>\$ 5,239</u>	<u>\$ 698</u>	13 %

Cost of Product Sales

Cost of product sales for the three months ended September 30, 2019, increased \$87 million, or 8%, compared with the same period in 2018. Cost of product sales for the nine months ended September 30, 2019, increased \$385 million, or 11%, compared with the same period in 2018. Ingalls cost of product sales decreased \$27 million for the three months ended September 30, 2019, primarily as a result of the volume changes described above. Ingalls cost of product sales increased \$13 million for the nine months ended September 30, 2019, primarily as a result of lower risk retirement in amphibious assault ships, partially offset by the lower volumes described above, as well as one time employee bonus payments in 2018 related to the Tax Act. Newport News cost of product sales increased \$89 million for the three months ended September 30, 2019, primarily as a result of the volume increases described above. Newport News cost of product sales increased \$296 million for the nine months ended September 30, 2019, primarily as a result of the volume increases described above and lower performance on the *Virginia* class (SSN 774) submarine program, partially offset by one time employee bonus payments in 2018 related to the Tax Act. Technical Solutions cost of product sales decreased \$15 million and \$23 million for the three and nine months ended September 30, 2019, respectively, primarily due to the lower volumes described above. Cost of product sales related to the Operating FAS/CAS Adjustment increased \$40 million and \$99 million for the three and nine months ended September 30, 2019, respectively, as described below.

Cost of product sales as a percentage of product sales increased from 74.9% for the three months ended September 30, 2018, to 80.6% for the three months ended September 30, 2019. This increase was primarily due to an unfavorable change in the Operating FAS/CAS Adjustment, a workers' compensation benefit in 2018, lower risk retirement on the *Legend* class NSC program, and year-to-year variances in contract mix, partially offset by improved performance on nuclear and environmental contracts. Cost of product sales as a percentage of product sales increased from 76.3% for the nine months ended September 30, 2018, to 82.4% for the nine months ended September 30, 2019. This increase was primarily due to an unfavorable change in the Operating FAS/CAS Adjustment, a workers' compensation benefit in 2018, lower risk retirement on the *San Antonio* class (LPD 17) program, lower performance on the *Virginia* class (SSN 774) submarine program, and year-to-year variances in contract mix, partially offset by one time employee bonus payments in 2018 related to the Tax Act.

Cost of Service Revenues

Cost of service revenues for the three months ended September 30, 2019, increased \$122 million, or 28%, compared with the same period in 2018. Cost of service revenues for the nine months ended September 30, 2019, increased \$347 million, or 27%, compared with the same period in 2018. Ingalls cost of service revenues for the

three months ended September 30, 2019, were consistent with the prior year primarily as a result of improved performance on surface combatant services, offset by the volume changes described above. Ingalls cost of service revenues decreased \$1 million for the nine months ended September 30, 2019, primarily as a result of improved performance on surface combatant services and the recognition in 2018 of a loss on a long-term design contract, partially offset by the volume changes described above. Newport News cost of service revenues increased \$14 million and \$90 million for the three and nine months ended September 30, 2019, primarily as a result of the volume changes described above. Technical Solutions cost of service revenues increased \$98 million for the three months ended September 30, 2019, primarily as a result of the higher volume described above. Technical Solutions cost of service revenues increased \$233 million for the nine months ended September 30, 2019, primarily as a result of the volume changes described above and a loss on a fleet support services contract, partially offset by one time employee bonus payments in 2018 related to the Tax Act. Cost of service revenues related to the Operating FAS/CAS Adjustment increased \$10 million and \$25 million for the three and nine months ended September 30, 2019, respectively, as described below.

Cost of service revenues as a percentage of service revenues increased from 81.0% for the three months ended September 30, 2018, to 82.5% for the three months ended September 30, 2019, primarily driven by unfavorable change in the Operating FAS/CAS Adjustment, partially offset by contract changes on submarine support services, improved performance on surface combatant services, and year-to-year variances in contract mix. Cost of service revenues as a percentage of service revenues increased from 82.4% for the nine months ended September 30, 2018, to 84.6% for the nine months ended September 30, 2019, primarily driven by an unfavorable change in the Operating FAS/CAS Adjustment, a loss on a fleet support services contract, and year-to-year variances in contract mix, partially offset by contract changes on submarine support services, one time employee bonus payments in 2018 related to the Tax Act, and the recognition in 2018 of a loss on a long-term design contract.

Income (Loss) from Operating Investments, Net

The activities of our operating investments are closely aligned with the operations of the segments holding the investments. We therefore record income related to earnings from equity method investments in our operating income.

Income from operating investments, net for the three months ended September 30, 2019, decreased \$2 million, primarily due to lower equity income from our nuclear and environmental joint ventures. Income from operating investments, net for the nine months ended September 30, 2019, increased \$3 million, primarily due to higher equity income from our nuclear and environmental joint ventures.

Other Income and Gains

Other income and gains for the nine months ended September 30, 2019, decreased \$14 million from the same period in 2018, primarily as a result of recoveries related to a settlement agreement at our Ingalls segment in 2018.

General and Administrative Expenses

In accordance with industry practice and the regulations that govern the cost accounting requirements for government contracts, most general and administrative expenses are considered allowable and allocable costs on government contracts. These costs are allocated to contracts in progress on a systematic basis, and contract performance factors include this cost component as an element of cost.

General and administrative expenses for the three months ended September 30, 2019, increased \$1 million from the same period in 2018, primarily driven by the addition of Fulcrum and G2, partially offset by lower current state income tax expense and overhead costs. General and administrative expenses for the nine months ended September 30, 2019, decreased \$45 million from the same period in 2018, primarily driven by lower current state income tax expense and overhead costs, partially offset by the addition of Fulcrum and G2 and unfavorable changes in non-current state income tax expense.

Operating Income

We consider operating income to be an important measure for evaluating our operating performance, and, as is typical in the industry, we define operating income as revenues less the related cost of producing the revenues and general and administrative expenses.

We internally manage our operations by reference to "segment operating income," which is defined as operating income before the Operating FAS/CAS Adjustment and non-current state income taxes, neither of which affects segment performance. Segment operating income is not a recognized measure under GAAP. When analyzing our operating performance, investors should use segment operating income in addition to, and not as an alternative for, operating income or any other performance measure presented in accordance with GAAP. It is a measure we use to evaluate our core operating performance. We believe segment operating income reflects an additional way of viewing aspects of our operations that, when viewed with our GAAP results, provides a more complete understanding of factors and trends affecting our business. We believe the measure is used by investors and is a useful indicator to measure our performance. Because not all companies use identical calculations, our presentation of segment operating income may not be comparable to similarly titled measures of other companies.

The following table reconciles operating income to segment operating income:

(\$ in millions)	Three Months Ended				Nine Months Ended			
	September 30		2019 over 2018		September 30		2019 over 2018	
	2019	2018	Dollars	Percent	2019	2018	Dollars	Percent
Operating income	\$ 214	\$ 290	\$ (76)	(26)%	\$ 550	\$ 738	\$ (188)	(25)%
Operating FAS/CAS Adjustment	(23)	(73)	50	68 %	(94)	(218)	124	57 %
Non-current state income taxes	—	—	—	— %	2	(5)	7	140 %
Segment operating income	<u>\$ 191</u>	<u>\$ 217</u>	<u>\$ (26)</u>	<u>(12)%</u>	<u>\$ 458</u>	<u>\$ 515</u>	<u>\$ (57)</u>	<u>(11)%</u>

Segment Operating Income

Segment operating income for the three months ended September 30, 2019, was \$191 million, a decrease of \$26 million from the same period in 2018. The decrease was primarily due to a workers' compensation benefit in 2018 and lower risk retirement on the *Legend* class NSC program, partially offset by contract changes on submarine support services. Segment operating income for the nine months ended September 30, 2019, was \$458 million, a decrease of \$57 million from the same period in 2018. The decrease was primarily due to lower risk retirement on the *San Antonio* class (LPD 17) program, a workers' compensation benefit in 2018, lower performance on the *Virginia* class (SSN 774) submarine program, as well as a loss on a fleet support services contract, and recoveries related to a settlement agreement in 2018, partially offset by higher volume at our Newport News segment, contract changes on submarine support services, higher equity income from our nuclear and environmental joint ventures, and one time employee bonus payments in 2018 related to the Tax Act.

Activity within each segment is discussed in Segment Operating Results below.

FAS/CAS Adjustment and Operating FAS/CAS Adjustment

The FAS/CAS Adjustment reflects the difference between expenses for pension and other postretirement benefits determined in accordance with GAAP ("FAS") and the expenses determined in accordance with U.S. Cost Accounting Standards ("CAS"). The Operating FAS/CAS Adjustment excludes the following components of net periodic benefit costs: interest cost, expected return on plan assets, amortization of prior service cost (credit) and actuarial loss (gain), and settlement and curtailment effects.

The components of the Operating FAS/CAS Adjustment were as follows:

(\$ in millions)	Three Months Ended				Nine Months Ended			
	September 30		2019 over 2018		September 30		2019 over 2018	
	2019	2018	Dollars	Percent	2019	2018	Dollars	Percent
FAS expense	\$ (35)	\$ (22)	\$ (13)	(59)%	\$ (105)	\$ (68)	\$ (37)	(54)%
CAS cost	61	114	(53)	(46)%	207	342	(135)	(39)%
FAS/CAS Adjustment	26	92	(66)	(72)%	102	274	(172)	(63)%
Non-operating retirement benefit	(3)	(19)	16	84 %	(8)	(56)	48	86 %
Operating FAS/CAS Adjustment	\$ 23	\$ 73	\$ (50)	(68)%	\$ 94	\$ 218	\$ (124)	(57)%

The Operating FAS/CAS Adjustment was a net benefit of \$23 million and \$73 million for the three months ended September 30, 2019 and 2018, respectively. The Operating FAS/CAS Adjustment was a net benefit of \$94 million and \$218 million for the nine months ended September 30, 2019 and 2018, respectively. The unfavorable changes in the Operating FAS/CAS Adjustment of \$50 million and \$124 million for the three and nine months ended September 30, 2019, respectively, compared with the same periods in 2018, were primarily driven by the more immediate recognition of higher interest rates under CAS.

Non-current State Income Taxes

Non-current state income taxes include deferred state income taxes, which reflect the change in deferred state tax assets and liabilities, and the tax expense or benefit associated with changes in state unrecognized tax benefits in the relevant period. These amounts are recorded within operating income. Current period state income tax expense is charged to contract costs and included in cost of sales and service revenues in segment operating income.

Non-current state income tax expense for the three months ended September 30, 2019, was less than \$1 million, compared to a non-current state income tax benefit of less than \$1 million for the same period in 2018. The unfavorable change in non-current state income taxes was driven by an increase in deferred state income tax expense primarily attributable to changes in the timing of contract taxable income. Non-current state income tax expense for the nine months ended September 30, 2019, was \$2 million, compared to a non-current state income tax benefit of \$5 million for the same period in 2018. The unfavorable change in non-current state income taxes was driven by an increase in deferred state income tax expense primarily attributable to changes in the timing of contract taxable income.

Interest Expense

Interest expense for the three and nine months ended September 30, 2019, increased \$4 million and \$8 million, respectively, compared with the same periods in 2018, primarily due to an increase in borrowings under our revolving credit facility.

Non-Operating Retirement Benefit

The non-operating retirement benefit includes the following components of net periodic benefit costs: interest cost, expected return on plan assets, amortization of prior service cost (credit) and actuarial loss (gain), and settlement and curtailment effects. For the three and nine months ended September 30, 2019, the unfavorable changes in the non-operating retirement benefit of \$16 million and \$48 million, respectively, were primarily driven by lower 2018 returns on plan assets.

Federal and Foreign Income Taxes

Our effective income tax rate on earnings from operations for the three months ended September 30, 2019, was 22.2%, compared with 22.4% for the same period in 2018. Our effective income tax rate on earnings from operations for the nine months ended September 30, 2019, was 21.7%, compared with 17.0% for the same period in 2018. The higher effective income tax rate for the nine months ended September 30, 2019, was primarily attributable to a claim for higher research and development tax credits for the post-spin-off 2011 through 2015 tax years recorded in 2018.

For the three months ended September 30, 2019, our effective income tax rate differed from the federal statutory rate primarily as a result of a non-recurring increase in tax expense for the true-up of estimated income taxes to the actual filed return. For the nine months ended September 30, 2019, our effective income tax rate differed from the federal statutory rate primarily as a result of an unfavorable adjustment to claims for research and development tax credits for prior tax years and a non-recurring increase in tax expense for the true-up of estimated income taxes to the actual filed return, partially offset by income tax benefits resulting from stock award settlement activity. For the three and nine months ended September 30, 2018, our effective income tax rates differed from the federal statutory rate primarily as a result of a claim for higher research and development tax credits for the post-spin-off 2011 through 2015 tax years. See Note 12: Income Taxes.

SEGMENT OPERATING RESULTS

Basis of Presentation

We are organized into three reportable segments: Ingalls, Newport News, and Technical Solutions.

The following table presents segment operating results:

(\$ in millions)	Three Months Ended				Nine Months Ended			
	September 30		2019 over 2018		September 30		2019 over 2018	
	2019	2018	Dollars	Percent	2019	2018	Dollars	Percent
Sales and Service Revenues								
Ingalls	\$ 647	\$ 694	\$ (47)	(7)%	\$ 1,853	\$ 1,908	\$ (55)	(3)%
Newport News	1,264	1,179	85	7 %	3,796	3,444	352	10 %
Technical Solutions	347	245	102	42 %	940	721	219	30 %
Intersegment eliminations	(39)	(35)	(4)	(11)%	(102)	(96)	(6)	(6)%
Sales and service revenues	<u>\$ 2,219</u>	<u>\$ 2,083</u>	<u>\$ 136</u>	<u>7 %</u>	<u>\$ 6,487</u>	<u>\$ 5,977</u>	<u>\$ 510</u>	<u>9 %</u>
Operating Income								
Ingalls	\$ 61	\$ 82	\$ (21)	(26)%	\$ 176	\$ 229	\$ (53)	(23)%
Newport News	109	119	(10)	(8)%	257	261	(4)	(2)%
Technical Solutions	21	16	5	31 %	25	25	—	— %
Segment operating income	<u>191</u>	<u>217</u>	<u>(26)</u>	<u>(12)%</u>	<u>458</u>	<u>515</u>	<u>(57)</u>	<u>(11)%</u>
Non-segment factors affecting operating income (loss)								
Operating FAS/CAS Adjustment	23	73	(50)	(68)%	94	218	(124)	(57)%
Non-current state income taxes	—	—	—	— %	(2)	5	(7)	(140)%
Operating income	<u>\$ 214</u>	<u>\$ 290</u>	<u>\$ (76)</u>	<u>(26)%</u>	<u>\$ 550</u>	<u>\$ 738</u>	<u>\$ (188)</u>	<u>(25)%</u>

KEY SEGMENT FINANCIAL MEASURES

Sales and Service Revenues

Period-to-period revenues reflect performance under new and ongoing contracts. Changes in sales and service revenues are typically expressed in terms of volume. Unless otherwise described, volume generally refers to increases (or decreases) in reported revenues due to varying production activity levels, delivery rates, or service levels on individual contracts. Volume changes will typically carry a corresponding income change based on the margin rate for a particular contract.

Segment Operating Income

Segment operating income reflects the aggregate performance results of contracts within a segment. Excluded from this measure are certain costs not directly associated with contract performance, such as the Operating FAS/CAS Adjustment and non-current state income taxes. Changes in segment operating income are typically expressed in

terms of volume, as discussed above, or performance. Performance refers to changes in contract margin rates. These changes typically relate to profit recognition associated with revisions to estimated costs at completion ("EAC") that reflect improved or deteriorated operating performance on that contract. Operating income changes are accounted for on a cumulative to date basis at the time an EAC change is recorded. Segment operating income may also be affected by, among other things, contract performance, the effects of workforce stoppages, the effects of natural disasters such as hurricanes, resolution of disputed items with the customer, recovery of insurance proceeds, and other discrete events. At the completion of a long-term contract, any originally estimated costs not incurred or reserves not fully utilized, such as warranty reserves, could also impact contract earnings. Where such items have occurred and the effects are material, a separate description is provided.

Cumulative Adjustments

For the three and nine months ended September 30, 2019 and 2018, favorable and unfavorable cumulative catch-up adjustments were as follows:

(\$ in millions)	Three Months Ended		Nine Months Ended	
	September 30		September 30	
	2019	2018	2019	2018
Gross favorable adjustments	\$ 64	\$ 61	\$ 158	\$ 163
Gross unfavorable adjustments	(20)	(27)	(101)	(64)
Net adjustments	\$ 44	\$ 34	\$ 57	\$ 99

For the three months ended September 30, 2019, favorable cumulative catch-up adjustments included contract changes on submarine support services and other individually insignificant adjustments. During the same period, none of the unfavorable cumulative catch-up adjustments were individually significant. For the nine months ended September 30, 2019, favorable cumulative catch-up adjustments were related to risk retirement on the *Legend* class NSC program, contract changes on submarine support services and other individually insignificant adjustments. During the same period, unfavorable cumulative catch-up adjustments included recognition of a forward loss on a fleet support services contract and other individually insignificant adjustments.

For the three months ended September 30, 2018, favorable cumulative catch-up adjustments were related to risk retirement on the *Legend* class NSC program and other individually insignificant adjustments. During the same period, none of the unfavorable cumulative catch-up adjustments were individually significant. For the nine months ended September 30, 2018, favorable cumulative catch-up adjustments were related to risk retirement on the *San Antonio* class (LPD 17) program, the *Legend* class NSC program, and the *Virginia* class (SSN 774) submarine program, as well as other individually insignificant adjustments. During the same period, none of the unfavorable cumulative catch-up adjustments were individually significant.

Ingalls

(\$ in millions)	Three Months Ended				Nine Months Ended			
	September 30		2019 over 2018		September 30		2019 over 2018	
	2019	2018	Dollars	Percent	2019	2018	Dollars	Percent
Sales and service revenues	\$ 647	\$ 694	\$ (47)	(7)%	\$ 1,853	\$ 1,908	\$ (55)	(3)%
Segment operating income	61	82	(21)	(26)%	176	229	(53)	(23)%
As a percentage of segment sales	9.4%	11.8%			9.5%	12.0%		

Sales and Service Revenues

Ingalls revenues for the three months ended September 30, 2019, decreased \$47 million from the same period in 2018, primarily driven by lower revenues in the *Legend* class NSC program and amphibious assault ships. Revenues on the *Legend* class NSC program decreased due to lower volumes on *Kimball* (NSC 7), *Midgett* (NSC 8), and *Stone* (NSC 9), partially offset by higher volumes on NSC 11 (unnamed). Amphibious assault ship revenues decreased as a result of lower volumes on *Tripoli* (LHA 7) and *Fort Lauderdale* (LPD 28), partially offset by higher volumes on *Harrisburg* (LPD 30) and *Bougainville* (LHA 8). Surface combatant revenues were consistent with the prior year due to higher volumes on *Ted Stevens* (DDG 128), USS *Fitzgerald* (DDG 62) repair and restoration,

Jeremiah Denton (DDG 129), and Jack H. Lucas (DDG 125), offset by lower volumes on *Delbert D. Black* (DDG 119), *Paul Ignatius* (DDG 117), *Frank E. Petersen Jr.* (DDG 121), and *Lenah H. Sutcliffe Higbee* (DDG 123).

Ingalls revenues for the nine months ended September 30, 2019, decreased \$55 million from the same period in 2018, primarily driven by lower revenues in the *Legend* class NSC program and surface combatants. Revenues on the *Legend* class NSC program decreased due to lower volumes on *Stone* (NSC 9), *Kimball* (NSC 7), and *Midgett* (NSC 8), partially offset by higher volumes on NSC 11 (unnamed) and NSC 10 (unnamed). Surface combatant revenues decreased as a result of lower volumes on *Delbert D. Black* (DDG 119), *Paul Ignatius* (DDG 117), *Frank E. Petersen Jr.* (DDG 121), and *Lenah H. Sutcliffe Higbee* (DDG 123), partially offset by higher volumes on USS *Fitzgerald* (DDG 62) repair and restoration, *Ted Stevens* (DDG 128), *Jeremiah Denton* (DDG 129), *Jack H. Lucas* (DDG 125), and *George M. Neal* (DDG 131). Amphibious assault ship revenues were consistent with the prior year due to higher volumes on *Bougainville* (LHA 8), *Harrisburg* (LPD 30), *Richard M. McCool Jr.* (LPD 29), and LPD Planning Yard and Life Cycle Engineering and Services, offset by lower volumes on *Tripoli* (LHA 7), *Fort Lauderdale* (LPD 28), and the delivered USS *Portland* (LPD 27), as well as lower risk retirement on the *San Antonio* class (LPD 17) program.

Segment Operating Income

Ingalls segment operating income for the three months ended September 30, 2019, was \$61 million, compared with \$82 million for the same period in 2018. The decrease was primarily due to lower risk retirement on the *Legend* class NSC program.

Ingalls segment operating income for the nine months ended September 30, 2019, was \$176 million, compared with \$229 million for the same period in 2018. The decrease was primarily due to lower risk retirement on the *San Antonio* class (LPD 17) program, as well as recoveries related to a settlement agreement in 2018, partially offset by one time employee bonus payments in 2018 related to the Tax Act.

Newport News

(\$ in millions)	Three Months Ended				Nine Months Ended			
	September 30		2019 over 2018		September 30		2019 over 2018	
	2019	2018	Dollars	Percent	2019	2018	Dollars	Percent
Sales and service revenues	\$ 1,264	\$ 1,179	\$ 85	7 %	\$ 3,796	\$ 3,444	\$ 352	10 %
Segment operating income	109	119	(10)	(8)%	257	261	(4)	(2)%
As a percentage of segment sales	8.6%	10.1%			6.8%	7.6%		

Sales and Service Revenues

Newport News revenues for the three months ended September 30, 2019, increased \$85 million, or 7%, from the same period in 2018, primarily driven by higher revenues in aircraft carriers and submarines. Aircraft carrier revenues increased primarily as a result of higher volumes on *Enterprise* (CVN 80) and the advance planning contract for the RCOH of USS *John C. Stennis* (CVN 74), partially offset by lower volumes on the RCOH of USS *George Washington* (CVN 73). Submarine revenues increased primarily as a result of higher volumes on the *Columbia* class and *Virginia* class (SSN 774) submarine programs. The higher volume on the *Virginia* class (SSN 774) submarine program was due to higher volumes on Block V boats, partially offset by lower volumes on Block III boats.

Newport News revenues for the nine months ended September 30, 2019, increased \$352 million, or 10%, from the same period in 2018, primarily driven by higher revenues in aircraft carriers and naval nuclear support services. Aircraft carrier revenues increased primarily as a result of higher volumes on *Enterprise* (CVN 80) and the advance planning contract for the RCOH of USS *John C. Stennis* (CVN 74), partially offset by lower volumes on *John F. Kennedy* (CVN 79) and the RCOH of USS *George Washington* (CVN 73). Naval nuclear support services revenues increased primarily as a result of contract changes on submarine support services and higher volume in facility maintenance services. Submarine revenues related to the *Virginia* class (SSN 774) submarine program were consistent with the prior year due to higher volumes on Block V and Block IV boats, offset by lower volumes on Block III boats.

Segment Operating Income

Newport News segment operating income for the three months ended September 30, 2019, was \$109 million, compared with \$119 million for the same period in 2018. The decrease was primarily due to a workers' compensation benefit in 2018, partially offset by contract changes on submarine support services.

Newport News segment operating income for the nine months ended September 30, 2019, was \$257 million, compared with \$261 million for the same period in 2018. The decrease was primarily due to a workers' compensation benefit in 2018 and lower performance on the *Virginia* class (SSN 774) submarine program, partially offset by contract changes on submarine support services and the higher volumes described above.

Technical Solutions

(\$ in millions)	Three Months Ended				Nine Months Ended			
	September 30		2019 over 2018		September 30		2019 over 2018	
	2019	2018	Dollars	Percent	2019	2018	Dollars	Percent
Sales and service revenues	\$ 347	\$ 245	\$ 102	42%	\$ 940	\$ 721	\$ 219	30%
Segment operating income (loss)	21	16	5	31%	25	25	—	—%
<i>As a percentage of segment sales</i>	<i>6.1%</i>	<i>6.5%</i>			<i>2.7%</i>	<i>3.5%</i>		

Sales and Service Revenues

Technical Solutions revenues for the three months ended September 30, 2019, increased \$102 million, or 42%, from the same period in 2018, due to higher MDIS revenues primarily attributable to the additions of Fulcrum and G2, as well as higher fleet support and oil and gas revenues.

Technical Solutions revenues for the nine months ended September 30, 2019, increased \$219 million, or 30%, from the same period in 2018, primarily due to higher MDIS revenues primarily attributable to the additions of Fulcrum and G2, as well as higher oil and gas and fleet support revenues.

Segment Operating Income

Technical Solutions segment operating income for the three months ended September 30, 2019, was \$21 million, compared with \$16 million for the same period in 2018. The increase was primarily due to improved performance on nuclear and environmental contracts.

Technical Solutions segment operating income for the nine months ended September 30, 2019, was \$25 million, compared with \$25 million for the same period in 2018. Operating income was consistent with the prior year primarily due to higher equity income from our nuclear and environmental joint ventures and one time employee bonus payments in 2018 related to the Tax Act, offset by a loss on a fleet support services contract.

BACKLOG

Total backlog as of September 30, 2019, and December 31, 2018, was approximately \$39 billion and \$23 billion, respectively. Total backlog includes both funded backlog (firm orders for which funding is contractually obligated by the customer) and unfunded backlog (firm orders for which funding is not currently contractually obligated by the customer). Backlog excludes unexercised contract options and unfunded IDIQ orders. For contracts having no stated contract values, backlog includes only the amounts committed by the customer.

The following table presents funded and unfunded backlog by segment as of September 30, 2019, and December 31, 2018:

(\$ in millions)	September 30, 2019			December 31, 2018		
	Funded	Unfunded	Total Backlog	Funded	Unfunded	Total Backlog
Ingalls	\$ 9,712	\$ 1,677	\$ 11,389	\$ 9,943	\$ 1,422	\$ 11,365
Newport News	7,570	19,179	26,749	6,767	4,144	10,911
Technical Solutions	520	570	1,090	339	380	719
Total backlog	\$ 17,802	\$ 21,426	\$ 39,228	\$ 17,049	\$ 5,946	\$ 22,995

Approximately 31% of the \$23 billion total backlog as of December 31, 2018, is expected to be converted into sales in 2019. U.S. Government orders comprised substantially all of the total backlog as of September 30, 2019, and December 31, 2018.

Awards

The value of new contract awards during the nine months ended September 30, 2019, was approximately \$22.6 billion. Significant new awards during the period included contracts for the detail design and construction of the *Gerald R. Ford* class (CVN 78) aircraft carriers *Enterprise* (CVN 80) and CVN 81 (unnamed) and the *San Antonio* class (LPD 17) amphibious transport dock *Harrisburg* (LPD 30).

LIQUIDITY AND CAPITAL RESOURCES

We endeavor to ensure the most efficient conversion of operating results into cash for deployment in operating our businesses, implementing our business strategy, and maximizing stockholder value. We use various financial measures to assist in capital deployment decision making, including net cash provided by operating activities and free cash flow. We believe these measures are useful to investors in assessing our financial performance.

The following table summarizes key components of cash flow provided by operating activities:

(\$ in millions)	Nine Months Ended September 30		2019 over 2018
	2019	2018	Dollars
Net earnings	\$ 400	\$ 624	\$ (224)
Depreciation and amortization	163	160	3
Provision for doubtful accounts	(5)	(4)	(1)
Stock-based compensation	19	27	(8)
Deferred income taxes	42	(1)	43
Retiree benefit funding less than (in excess of) expense	56	(468)	524
Trade working capital decrease (increase)	(345)	(72)	(273)
Net cash provided by operating activities	\$ 330	\$ 266	\$ 64

Cash Flows

We discuss below our major operating, investing, and financing activities for the nine months ended September 30, 2019 and 2018, as classified on our unaudited condensed consolidated statements of cash flows.

Operating Activities

Cash provided by operating activities for the nine months ended September 30, 2019, was \$330 million, compared with \$266 million provided by operating activities for the same period in 2018. The favorable change in operating cash flow was primarily due to lower contributions to retiree benefit plans, partially offset by changes in trade working capital and higher cash paid for income taxes. The change in trade working capital was primarily driven by the timing of receipts of accounts receivable and payments of accounts payable.

For the nine months ended September 30, 2019, we made discretionary contributions to our qualified defined benefit pension plans totaling \$21 million, compared with \$508 million of discretionary contributions for the same period in 2018. As of September 30, 2019, we anticipate no further significant cash contributions to our qualified defined benefit pension plans in 2019.

We expect cash generated from operations in combination with our current cash and cash equivalents, as well as existing credit facilities, to be more than sufficient to service debt, meet contractual obligations, and finance capital expenditures for at least the next 12 months.

Investing Activities

Cash used in investing activities for the nine months ended September 30, 2019, was \$470 million, compared with \$267 million used in investing activities for the same period in 2018. The change in investing cash used was driven by the acquisition of Fulcrum. For 2019, we expect our capital expenditures for maintenance and sustainment to be approximately 2% to 2.5% and our discretionary capital expenditures to be approximately 3% to 3.5% of annual revenues.

Financing Activities

Cash used in financing activities for the nine months ended September 30, 2019, was \$68 million, compared with \$632 million used in financing activities for the same period in 2018. The change in financing cash was primarily due to a decrease of \$310 million in common stock repurchases, \$264 million of net proceeds from revolving credit facility borrowings, and a decrease of \$2 million in employee taxes on certain share-based payment arrangements, partially offset by a \$12 million increase in cash dividend payments.

Free Cash Flow

Free cash flow represents cash provided by (used in) operating activities less capital expenditures net of related grant proceeds. Free cash flow is not a measure recognized under GAAP. Free cash flow has limitations as an analytical tool and should not be considered in isolation from, or as a substitute for, analysis of our results as reported under GAAP. We believe free cash flow is an important measure for our investors because it provides them insight into our current and period-to-period performance and our ability to generate cash from continuing operations. We also use free cash flow as a key operating metric in assessing the performance of our business and as a key performance measure in evaluating management performance and determining incentive compensation. Free cash flow may not be comparable to similarly titled measures of other companies.

The following table reconciles net cash provided by operating activities to free cash flow:

(\$ in millions)	Nine Months Ended September 30		2019 over 2018
	2019	2018	Dollars
Net cash provided by operating activities	\$ 330	\$ 266	\$ 64
Less capital expenditures:			
Capital expenditure additions	(349)	(293)	(56)
Grant proceeds for capital expenditures	71	33	38
Free cash flow	\$ 52	\$ 6	\$ 46

Free cash flow for the nine months ended September 30, 2019, increased \$46 million from the same period in 2018, primarily due to lower contributions to retiree benefit plans, partially offset by changes in trade working capital, higher capital expenditures, and higher cash paid for income taxes.

Governmental Regulation and Supervision

The U.S. Government has the ability, pursuant to regulations relating to contractor business systems, to decrease or withhold contract payments if it determines significant deficiencies exist in one or more such systems. As of

September 30, 2019 and 2018, the cumulative amounts of payments withheld by the U.S. Government under our contracts subject to these regulations were not material to our liquidity or cash flows.

Off-Balance Sheet Arrangements

In the ordinary course of business, we use standby letters of credit issued by commercial banks and surety bonds issued by insurance companies principally to support our self-insured workers' compensation plans. As of September 30, 2019, we had \$22 million in issued but undrawn standby letters of credit and \$273 million of surety bonds outstanding.

ACCOUNTING STANDARDS UPDATES

See Note 3: Accounting Standards Updates in Part I, Item 1 for information related to accounting standards updates.

FORWARD-LOOKING STATEMENTS AND PROJECTIONS

Statements in this Quarterly Report on Form 10-Q and in our other filings with the Securities and Exchange Commission ("SEC"), as well as other statements we may make from time to time, other than statements of historical fact, constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements involve risks and uncertainties that could cause our actual results to differ materially from those expressed in these statements. Factors that may cause such differences include:

- Changes in government and customer priorities and requirements (including government budgetary constraints, shifts in defense spending, and changes in customer short-range and long-range plans);
- Our ability to estimate our future contract costs and perform our contracts effectively;
- Changes in procurement processes and government regulations and our ability to comply with such requirements;
- Our ability to deliver our products and services at an affordable life cycle cost and compete within our markets;
- Natural and environmental disasters and political instability;
- Our ability to execute our strategic plan, including with respect to share repurchases, dividends, capital expenditures, and strategic acquisitions;
- Adverse economic conditions in the United States and globally;
- Changes in key estimates and assumptions regarding our pension and retiree health care costs;
- Security threats, including cyber security threats, and related disruptions; and
- Other risk factors discussed herein and in our other filings with the SEC.

There may be other risks and uncertainties that we are unable to predict at this time or that we currently do not expect to have a material adverse effect on our business, and we undertake no obligation to update or revise any forward-looking statements. You should not place undue reliance on any forward looking statements that we may make.

GLOSSARY OF PROGRAMS

Included below are brief descriptions of some of the programs discussed in this Quarterly Report on Form 10-Q.

Program Name	Program Description
<i>America</i> class (LHA 6) amphibious assault ships	Design and build large deck amphibious assault ships that provide forward presence and power projection as an integral part of joint, interagency and multinational maritime expeditionary forces. The <i>America</i> class (LHA 6) ships, together with the <i>Wasp</i> class (LHD 1) ships, are the successors to the decommissioned <i>Tarawa</i> class (LHA 1) ships. The <i>America</i> class (LHA 6) ships optimize aviation operations and support capabilities. We delivered USS <i>America</i> (LHA 6) in April 2014, <i>Tripoli</i> (LHA 7) is scheduled for delivery in 2019, and we are currently constructing <i>Bougainville</i> (LHA 8).
<i>Arleigh Burke</i> class (DDG 51) destroyers	Build guided missile destroyers designed for conducting anti-air, anti-submarine, anti-surface, and strike operations. The Aegis-equipped <i>Arleigh Burke</i> class (DDG 51) destroyers are the U.S. Navy's primary surface combatant, and have been constructed in variants, allowing technological advances during construction. In 2016 we delivered USS <i>John Finn</i> (DDG 113), in 2017 we delivered <i>Ralph Johnson</i> (DDG 114), and in 2019 we delivered <i>Paul Ignatius</i> (DDG 117). We have contracts to construct the following <i>Arleigh Burke</i> class (DDG 51) destroyers: <i>Delbert D. Black</i> (DDG 119), <i>Frank E. Petersen Jr.</i> (DDG 121), <i>Lenah H. Sutcliffe Higbee</i> (DDG 123), <i>Jack H. Lucas</i> (DDG 125), <i>Ted Stevens</i> (DDG 128), <i>Jeremiah Denton</i> (DDG 129), <i>George M. Neal</i> (DDG 131), <i>Sam Nunn</i> (DDG 133), DDG 135 (unnamed), and DDG 137 (unnamed).
Carrier RCOH	Perform refueling and complex overhaul ("RCOH") of nuclear-powered aircraft carriers, which is required at the mid-point of their 50-year life cycle. USS <i>Abraham Lincoln</i> (CVN 72) was redelivered to the U.S. Navy in the second quarter of 2017 and USS <i>George Washington</i> (CVN 73) arrived at Newport News for the start of its RCOH in August 2017.
<i>Columbia</i> class (SSBN 826) submarines	Newport News is participating in designing the <i>Columbia</i> class submarine as a replacement for the current aging <i>Ohio</i> class nuclear ballistic missile submarines, which were first introduced into service in 1981. The <i>Ohio</i> class SSBN includes 14 nuclear ballistic missile submarines and four nuclear cruise missile submarines. The <i>Columbia</i> class program plan of record is to construct 12 new ballistic missile submarines. The U.S. Navy has initiated the design process for the new class of submarines, and, in early 2017, the DoD signed the acquisition decision memorandum approving the <i>Columbia</i> class program's Milestone B, which formally authorizes the program's entry into the engineering and manufacturing development phase. We perform design work as a subcontractor to Electric Boat, and we have entered into a teaming agreement with Electric Boat to build modules for the entire <i>Columbia</i> class submarine program that leverages our <i>Virginia</i> class (SSN 774) experience. We have been awarded contracts from Electric Boat to begin integrated product and process development and provide long-lead-time material and advance construction for the <i>Columbia</i> class (SSBN 826) program. Construction of the first <i>Columbia</i> class (SSBN 826) submarine is expected to begin in 2021.

Fleet support services	Provide comprehensive life-cycle sustainment services to the U.S. Navy fleet and other DoD and commercial maritime customers. We provide services including maintenance, modernization, and repair on all ship classes; naval architecture, marine engineering, and design; integrated logistics support; technical documentation development; warehousing, asset management, and material readiness; operational and maintenance training development and delivery; software design and development; IT infrastructure support and data delivery and management; and cyber security and information assurance. We provide undersea vehicle and specialized craft development and prototyping services.
USS <i>Gerald R. Ford</i> class (CVN 78) aircraft carriers	Design and construction for the <i>Ford</i> class program, which is the aircraft carrier replacement program for the decommissioned <i>Enterprise</i> (CVN 65) and <i>Nimitz</i> class (CVN 68) aircraft carriers. USS <i>Gerald R. Ford</i> (CVN 78), the first ship of the <i>Ford</i> class, was delivered to the U.S. Navy in the second quarter of 2017. In June 2015, we were awarded a contract for the detail design and construction of <i>John F. Kennedy</i> (CVN 79), following several years of engineering, advance construction, and purchase of long-lead time components and material. In addition, we have received awards for detail design and construction of <i>Enterprise</i> (CVN 80) and CVN 81 (unnamed.) This category also includes the class' non-recurring engineering. The class is expected to bring improved warfighting capability, quality of life improvements for sailors, and reduced life cycle costs.
<i>Legend</i> class National Security Cutter	Design and build the U.S. Coast Guard's National Security Cutters ("NSCs"), the largest and most technically advanced class of cutter in the U.S. Coast Guard. The NSC is equipped to carry out maritime homeland security, maritime safety, protection of natural resources, maritime mobility, and national defense missions. The plan is for a total of 11 ships, of which the first eight ships have been delivered. <i>Stone</i> (NSC 9), NSC 10 (unnamed), and NSC 11 (unnamed) are currently under construction.
MDIS services	Provide services to DoD, intelligence, and federal civilian customers. Services are performed in six major portfolio areas: modeling, simulation and training, information technology and software application, artificial intelligence and data analytics, mission engineering and operations support, logistics and life cycle management, and cyber space operations.
Naval nuclear support services	Provide services to and in support of the U.S. Navy, ranging from services supporting the Navy's carrier and submarine fleets to maintenance services at U.S. Navy training facilities. Naval nuclear support services include design, construction, maintenance, and disposal activities for in service U.S. Navy nuclear ships worldwide through mobile and in-house capabilities. Services include maintenance services on nuclear reactor prototypes.
Nuclear and environmental services	Provide services in nuclear management and operations, and nuclear and non-nuclear fabrication and repair. We provide site management, nuclear and industrial facilities operations and maintenance, decontamination and decommissioning, and radiological and hazardous waste management services. We provide services, including fabrication, equipment repair, and technical engineering services. We participate in several joint ventures, including N3B, MSTS, and SRNS. N3B was awarded the Los Alamos Legacy Cleanup Contract at the DoE/National Nuclear Security Administration's Los Alamos National Laboratory. MSTS was awarded a contract for site management and operations at the Nevada National Security Site. SRNS provides site management and operations at the DoE's Savannah River Site near Aiken, South Carolina.

Oil and gas services

Deliver engineering, procurement, and construction management services to the oil and gas industry for major pipeline, production, and treatment facilities. These services include full life-cycle services for domestic and international projects, from concept identification through detail design, execution and construction, and decommissioning. Related field services include survey, inspection, commissioning and start-up, operations and maintenance, and optimization and debottlenecking.

San Antonio class (LPD 17) amphibious transport dock ships

Design and build amphibious transport dock ships, which are warships that embark, transport, and land elements of a landing force for a variety of expeditionary warfare missions, and also serve as the secondary aviation platform for Amphibious Readiness Groups. The *San Antonio* class (LPD 17) is the newest addition to the U.S. Navy's 21st century amphibious assault force, and these ships are a key element of the U.S. Navy's seabase transformation. In 2013, we delivered USS *Somerset* (LPD 25), in 2016, we delivered USS *John P. Murtha* (LPD 26), and, in 2017, we delivered USS *Portland* (LPD 27). We are currently constructing *Fort Lauderdale* (LPD 28), *Richard M. McCool Jr.* (LPD 29), and *Harrisburg* (LPD 30).

The decommissioned *Enterprise* (CVN 65)

Defuel and inactivate the world's first nuclear-powered aircraft carrier, which began in 2013. The inactivation was completed in the second quarter of 2018.

Virginia class (SSN 774) fast attack submarines

Construct attack submarines as the principal subcontractor to Electric Boat. The *Virginia* class (SSN 774) is a post-Cold War design tailored to excel in a wide range of warfighting missions, including anti-submarine and surface ship warfare; special operation forces; strike; intelligence, surveillance, and reconnaissance; carrier and expeditionary strike group support; and mine warfare.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

We are exposed to market risk, primarily related to interest rates and foreign currency exchange rates.

Interest Rates - Our financial instruments subject to interest rate risk include floating rate borrowings under our credit facility. As of September 30, 2019, we had \$264 million of floating rate debt outstanding under our \$1,250 million revolving credit facility. Based on the amounts outstanding under our credit facility as of September 30, 2019, an increase of 1% in interest rates would increase the interest expense on our debt by approximately \$3 million on an annual basis.

Foreign Currency - We currently have, and in the future may enter into, foreign currency forward contracts to manage foreign currency exchange rate risk related to payments to suppliers denominated in foreign currencies. As of September 30, 2019, the fair values of our outstanding foreign currency forward contracts were not significant.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of September 30, 2019. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that, as of September 30, 2019, the Company's disclosure controls and procedures were effective to ensure that information required to be disclosed in reports the Company files or submits under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and (ii) accumulated and communicated to management to allow their timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

During the three months ended September 30, 2019, no change occurred in the Company's internal control over financial reporting that materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

The Company implemented a new Enterprise Resource Planning ("ERP") system at its Ingalls segment in the first quarter of 2019. The Company followed a system implementation process that required significant pre-implementation planning, design, and testing. The Company also conducted and will continue to conduct extensive post-implementation monitoring and process modifications to ensure that internal controls over financial reporting are properly designed. The Company does not expect this system implementation to have a material effect on its internal controls over financial reporting.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings

We have provided information about legal proceedings in which we are involved in the unaudited condensed consolidated financial statements in Part I, Item 1, which is incorporated herein by reference. In addition to the matters disclosed in Part I, Item 1, we are a party to various investigations, lawsuits, claims, and other legal proceedings that arise in the ordinary course of our business. Based on information available to us, we do not believe at this time that any of such other matters will individually, or in the aggregate, have a material adverse effect on our financial condition, results of operations, or cash flows. For further information on the risks we face from existing and future investigations, lawsuits, claims, and other legal proceedings, please see "Risk Factors" in Item 1A below.

Item 1A. Risk Factors

The Company has no material changes to report from the risk factors described in "Risk Factors" in its Annual Report on Form 10-K for the year ended December 31, 2018.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

In November 2017, the Company's board of directors authorized an increase in the Company's stock repurchase program from \$1.2 billion to \$2.2 billion. On November 5, 2019, the Company's board of directors authorized an increase in the Company's stock repurchase program from \$2.2 billion to \$3.2 billion and an extension of the term of the program to October 31, 2024. Repurchases are made from time to time at management's discretion in accordance with applicable federal securities laws. All repurchases of HII common stock have been recorded as treasury stock. The following table summarizes information relating to purchases made by or on behalf of the Company of shares of the Company's common stock during the quarter ended September 30, 2019.

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Program	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Program (in millions) ¹
July 1, 2019 to July 31, 2019	29,872	\$ 230.15	29,872	\$ 345.1
August 1, 2019 to August 31, 2019	155,799	206.96	155,799	312.8
September 1, 2019 to September 30, 2019	135,886	211.88	135,886	284.0
Total	321,557	\$ 211.19	321,557	\$ 284.0

¹ From the stock repurchase program's inception through September 30, 2019, we purchased 12,205,691 shares at an average price of \$156.97 per share for a total of \$1.9 billion.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

None.

Item 5. Other Information

None.

Item 6. Exhibits

- 3.1 [Restated Certificate of Incorporation of Huntington Ingalls Industries, Inc., filed March 30, 2011 \(incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K filed on April 4, 2011\).](#)
- 3.2 [Certificate of Amendment to the Restated Certificate of Incorporation of Huntington Ingalls Industries, Inc., dated May 28, 2014 \(incorporated by reference to Exhibit 3.2 to the Company's Quarterly Report on Form 10-Q filed on August 7, 2014\).](#)
- 3.3 [Certificate of Amendment to the Restated Certificate of Incorporation of Huntington Ingalls Industries, Inc., dated May 21, 2015 \(incorporated by reference to Exhibit 3.3 to the Company's Quarterly Report on Form 10-Q filed on August 6, 2015\).](#)
- 3.4 [Restated Bylaws of Huntington Ingalls Industries, Inc. \(incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K filed on February 1, 2016\).](#)
- 4.1 [Second supplemental indenture, dated as of August 27, 2019, to the indenture, dated as of November 17, 2015, among Huntington Ingalls Industries, Inc., the guarantors party thereto, and The Bank of New York Mellon, as trustee.](#)
- 4.2 [First supplemental indenture, dated as of August 27, 2019, to the indenture, dated as of December 1, 2017, among Huntington Ingalls Industries, Inc., the guarantors party thereto, and Wells Fargo Bank, National Association, as trustee.](#)
- 31.1 [Certification of the Chief Executive Officer Pursuant to Exchange Act Rule 13a-14\(a\)/15d-14\(a\), as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.](#)
- 31.2 [Certification of the Chief Financial Officer Pursuant to Exchange Act Rule 13a-14\(a\)/15d-14\(a\), as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.](#)
- 32.1 [Certificate of the Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.](#)
- 32.2 [Certificate of the Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.](#)
- 101 The following financial information for the Company, formatted in XBRL (Extensible Business Reporting Language): (i) the Condensed Consolidated Statements of Operations and Comprehensive Income, (ii) the Condensed Consolidated Statements of Financial Position, (iii) the Condensed Consolidated Statements of Cash Flows, (iv) the Condensed Consolidated Statements of Changes in Equity, and (v) the Notes to Condensed Consolidated Financial Statements.
- 104 The cover page from the Company's Quarterly Report on Form 10-Q, formatted in Inline XBRL and contained in Exhibit 101.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: November 7, 2019

Huntington Ingalls Industries, Inc.
(Registrant)

By: /s/ Nicolas Schuck

Nicolas Schuck

Corporate Vice President, Controller and Chief Accounting Officer
(Duly Authorized Officer and Principal Accounting Officer)

SECOND SUPPLEMENTAL INDENTURE

dated as of August 27, 2019

among

Huntington Ingalls Industries, Inc.,

The Guarantor(s) Party Hereto

and

The Bank of New York Mellon,
as Trustee

5.000% Senior Notes due 2025

THIS SECOND SUPPLEMENTAL INDENTURE (this “**Second Supplemental Indenture**”), entered into as of August 27, 2019, among Huntington Ingalls Industries, Inc., a Delaware corporation (the “**Company**”), G2, Inc., a Maryland corporation (“**G2**”), Fulcrum IT Services, LLC, a Virginia limited liability company (“**Fulcrum**”), The PTR Group, LLC, a Virginia limited liability company (“**PTR**”, and each of G2, Fulcrum, and PTR, an “**Undersigned**”), and The Bank of New York Mellon, as trustee (the “**Trustee**”).

RECITALS

WHEREAS, the Company, the Guarantors party thereto and the Trustee entered into the Indenture, dated as of November 17, 2015, as modified by the First Supplemental Indenture, dated as of February 17, 2017 (as modified, the “**Indenture**”), relating to the Company’s 5.000% Senior Notes due 2025 (the “**Notes**”);

WHEREAS, as a condition to the Trustee entering into the Indenture and the purchase of the Notes by the Holders, the Company agreed pursuant to the Indenture to cause Domestic Subsidiaries that Guarantee, and any Wholly Owned Domestic Subsidiaries that Incur, Debt under the Credit Agreement or that Guarantee or Incur Debt after the Issue Date under any other Credit Facility to enter into this Second Supplemental Indenture to provide Guarantees.

AGREEMENT

NOW, THEREFORE, in consideration of the premises and mutual covenants herein contained and intending to be legally bound, the parties to this Second Supplemental Indenture hereby agree as follows:

Section 1. Capitalized terms used herein and not otherwise defined herein are used as defined in the Indenture.

Section 2. Each Undersigned, by its execution of this Second Supplemental Indenture, agrees to be a Guarantor under the Indenture and to be bound by the terms of the Indenture applicable to Guarantors, including, but not limited to, Article 10 thereof.

Section 3. This Second Supplemental Indenture shall be governed by and construed in accordance with the laws of the State of New York.

Section 4. This Second Supplemental Indenture may be signed in various counterparts which together will constitute one and the same instrument.

Section 5. This Second Supplemental Indenture is an amendment supplemental to the Indenture and the Indenture and this Second Supplemental Indenture will henceforth be read together.

Section 6. The Trustee shall not be responsible in any manner whatsoever for or in respect of the validity or sufficiency of this Second Supplemental Indenture or for or in respect of the recitals contained herein, all of which recitals are made solely by the other parties hereto.

[Signature Page to Second Supplemental Indenture (5.000% Notes)]

IN WITNESS WHEREOF, the parties hereto have caused this Second Supplemental Indenture to be duly executed as of the date first above written.

Huntington Ingalls Industries, Inc., as Issuer

By: _____
Name:
Title:

[signatures continue on the following page.]

G2, Inc., as a Guarantor

By: _____
Name:
Title:

[signatures continue on the following page.]

Fulcrum IT Services, LLC, as a Guarantor

By: _____
Name:
Title:

[signatures continue on the following page.]

The PTR Group, LLC, as a Guarantor

By: _____
Name:
Title:

[signatures continue on the following page.]

The Bank of New York Mellon, as Trustee

By: _____
Name:
Title:

FIRST SUPPLEMENTAL INDENTURE

dated as of August 27, 2019

among

Huntington Ingalls Industries, Inc.,

The Guarantor(s) Party Hereto

and

Wells Fargo Bank, National Association,
as Trustee

3.483% Senior Notes due 2027

THIS FIRST SUPPLEMENTAL INDENTURE (this “**First Supplemental Indenture**”), entered into as of August 27, 2019, among Huntington Ingalls Industries, Inc., a Delaware corporation (the “**Company**”), G2, Inc., a Maryland corporation (“**G2**”), Fulcrum IT Services, LLC, a Virginia limited liability company (“**Fulcrum**”), The PTR Group, LLC, a Virginia limited liability company (“**PTR**”, and each of G2, Fulcrum, and PTR, an “**Undersigned**”), and Wells Fargo Bank, National Association, as trustee (the “**Trustee**”).

RECITALS

WHEREAS, the Company, the Guarantors party thereto and the Trustee entered into the Indenture, dated as of December 1, 2017 (the “**Indenture**”), relating to the Company’s 3.483% Senior Notes due 2027 (the “**Notes**”);

WHEREAS, as a condition to the Trustee entering into the Indenture and the purchase of the Notes by the Holders, the Company agreed pursuant to the Indenture to cause Domestic Subsidiaries that Guarantee, and any Wholly Owned Domestic Subsidiaries that Incur, Debt under the Credit Agreement or that Guarantee or Incur Debt after the Issue Date under any other Credit Facility to enter into this First Supplemental Indenture to provide Guarantees.

AGREEMENT

NOW, THEREFORE, in consideration of the premises and mutual covenants herein contained and intending to be legally bound, the parties to this First Supplemental Indenture hereby agree as follows:

Section 1. Capitalized terms used herein and not otherwise defined herein are used as defined in the Indenture.

Section 2. Each Undersigned, by its execution of this First Supplemental Indenture, agrees to be a Guarantor under the Indenture and to be bound by the terms of the Indenture applicable to Guarantors, including, but not limited to, Article 10 thereof.

Section 3. This First Supplemental Indenture shall be governed by and construed in accordance with the laws of the State of New York.

Section 4. This First Supplemental Indenture may be signed in various counterparts which together will constitute one and the same instrument.

Section 5. This First Supplemental Indenture is an amendment supplemental to the Indenture and the Indenture and this First Supplemental Indenture will henceforth be read together.

Section 6. The Trustee shall not be responsible in any manner whatsoever for or in respect of the validity or sufficiency of this First Supplemental Indenture or for or in respect of the recitals contained herein, all of which recitals are made solely by the other parties hereto.

[Signature Page to First Supplemental Indenture (3.483% Notes)]

IN WITNESS WHEREOF, the parties hereto have caused this First Supplemental Indenture to be duly executed as of the date first above written.

Huntington Ingalls Industries, Inc., as Issuer

By: _____
Name:
Title:

[signatures continue on the following page.]

G2, Inc., as a Guarantor

By: _____
Name:
Title:

[signatures continue on the following page.]

Fulcrum IT Services, LLC, as a Guarantor

By: _____
Name:
Title:

[signatures continue on the following page.]

The PTR Group, LLC, as a Guarantor

By: _____
Name:
Title:

[signatures continue on the following page.]

Wells Fargo Bank, National Association, as Trustee

By: _____
Name:
Title:

**CERTIFICATION PURSUANT TO
EXCHANGE ACT RULE 13A-14(A)/15D-14(A)
AS ADOPTED PURSUANT TO SECTION 302
OF THE SARBANES-OXLEY ACT OF 2002**

I, C. Michael Petters, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Huntington Ingalls Industries, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 7, 2019

/s/ C. Michael Petters

C. Michael Petters

President and Chief Executive Officer

**CERTIFICATION PURSUANT TO
EXCHANGE ACT RULE 13A-14(A)/15D-14(A)
AS ADOPTED PURSUANT TO SECTION 302
OF THE SARBANES-OXLEY ACT OF 2002**

I, Christopher D. Kastner, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Huntington Ingalls Industries, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 7, 2019

/s/ Christopher D. Kastner

Christopher D. Kastner

Executive Vice President, Business Management and Chief
Financial Officer

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Huntington Ingalls Industries, Inc. (the "company") on Form 10-Q for the period ended September 30, 2019 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, C. Michael Petters, the President and Chief Executive Officer of the company, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to my knowledge, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the company.

Date: November 7, 2019

/s/ C. Michael Petters

C. Michael Petters

President and Chief Executive Officer

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Huntington Ingalls Industries, Inc. (the "company") on Form 10-Q for the period ended September 30, 2019 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Christopher D. Kastner, Corporate Vice President, Business Management and Chief Financial Officer of the company, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to my knowledge, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the company.

Date: November 7, 2019

/s/ Christopher D. Kastner

Christopher D. Kastner

Executive Vice President, Business Management and
Chief Financial Officer