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× EXAMINATION OF FINANCIAL STATEMENTS OF  
THE FEDERAL PRISON INDUSTRIES, INC., DE-  
PARTMENT OF JUSTICE, FOR FISCAL YEAR 1973

COMMUNICATION

FROM

COMPTROLLER GENERAL OF THE  
UNITED STATES

TRANSMITTING

A REPORT ON THE EXAMINATION OF FINANCIAL  
STATEMENTS OF THE FEDERAL PRISON INDUSTRIES,  
INC., DEPARTMENT OF JUSTICE, FOR FISCAL YEAR  
1973, PURSUANT TO 31 U.S.C. 841



MARCH 19, 1974.—Referred to the Committee on Government  
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COMPTROLLER GENERAL OF THE UNITED STATES  
WASHINGTON, D.C. 20548

B-114826

March 19, 1974

C1 The Honorable Carl Albert  
Speaker of the House of Representatives

Dear Mr. Speaker:

1 This is our report on the examination of the financial  
statements of the Federal Prison Industries, Inc., Department  
of Justice, for the fiscal year ended June 30, 1973.

We made our examination pursuant to the Government  
Corporation Control Act (31 U.S.C. 841).

C2 We are also sending this report to the President of  
the Senate. Copies are being sent to the Director, Office  
of Management and Budget, and the Attorney General.

Sincerely yours,

*Robert B. Staack*

Comptroller General  
of the United States

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ABBREVIATIONS

BOP	Bureau of Prisons
GAO	General Accounting Office

## D I G E S T

### WHY THE EXAMINATION WAS MADE

The Government Corporation Control Act requires the Comptroller General to examine annually the financial activities of the Federal Prison Industries, Inc.

#### Background

The Federal Prison Industries, Inc., a wholly owned Government corporation created June 23, 1934, functions within the Department of Justice under the general direction and supervision of the Attorney General. The primary goal of the corporation is to offer inmates in Federal prisons training and work experience in skills that provide opportunity for employment upon release.

### OPINION ON FINANCIAL STATEMENTS

In GAO's opinion the corporation's financial statements included in this report present fairly its financial position at June 30, 1973, and the results of its operations and changes in financial position for the year then ended, in conformity with principles and standards of accounting prescribed for executive agencies by the Comptroller General of the United States applied on a basis consistent with that of the preceding year--except for the change in the method for eliminating interindustry profit from inventories, with which we concur.

### OTHER MATTERS OF INTEREST

During fiscal year 1973 the corporation conducted 52 industrial operations at 21 Federal institutions. These operations ranged from the manufacture of gloves, brushes, and brooms to automatic data processing and printing services. (See pp. 3 and 4.)

The corporation's sales to Government agencies for the year amounted to almost \$54 million. Net industrial profits resulting from these sales totaled \$6.6 million, an increase of \$245,577 over the previous year. An analysis of distribution of profits shows that about \$5.2 million, including depreciation, was used to support vocational training programs and almost \$1 million was used for meritorious and accident compensation to inmates. (See p. 5.)

Profits retained amounted to \$384,039, a decrease of about \$11,000 from that of the preceding year. (See p. 5.)

The corporation's cash available for operations declined about 28 percent from the preceding year to \$4.6 million at June 30, 1973. Available cash further decreased to \$2.5 million in October 1973. Corporate officials initiated an immediate action plan to improve the

declining cash position (See p. 5.)

RECOMMENDATIONS

This report contains no recommendations.

MATTERS FOR CONSIDERATION BY THE CONGRESS

This report is submitted to the Congress as required by the Government Corporation Control Act.

## CHAPTER 1

### INTRODUCTION

The Federal Prison Industries, Inc., a wholly owned Government corporation created pursuant to the act of June 23, 1934 (48 Stat. 1211, 18 U.S.C. 4121), functions within the Department of Justice under the general direction and supervision of the Attorney General. The primary goal of the corporation is to offer inmates in Federal prisons training and work experience in skills that provide for employment opportunities upon release.

The operating policies of the corporation are prescribed by a board of directors composed of six members representing retailers and consumers, the Secretary of Defense, labor, industry, agriculture, and the Attorney General. These members are appointed for indefinite terms by the President of the United States and serve without compensation. These members and the principal officials responsible for administering the day-to-day operations of the corporation are included in appendix I.

Under the act which created the corporation, Government agencies are required to purchase, at prices not exceeding current market prices, such products of the industries as meet their requirements and as may be available. The corporation's board of directors has established the policy that prices shall not be materially below current market prices.

During fiscal year 1973 the corporation had 52 industrial operations at 21 Federal institutions. Types of industries ranged from the manufacture of gloves, brushes, and brooms to automatic data processing and printing services. Total inmate employment for the fiscal year ended June 30, 1973, averaged nearly 5,000, or about 21 percent of the total inmate population.

### EVALUATION OF SUCCESS IN REHABILITATING INMATES

The Federal penal system's training, education, and industrial programs are conducted by the Bureau of Prisons (BOP) and the corporation under the auspices of the Department of Justice. BOP operates from appropriated money,

whereas the corporation generates its own funds through industrial operations. Certain BOP functions, such as the vocational training program which is subject to fiscal limitations imposed by the Congress, are financed from corporate profits.

In November 1973 we issued a report entitled "Rehabilitating Inmates of Federal Prisons: Special Programs Help, But Not Enough" (B-133223). The report evaluated the success of the prison system's programs for preparing Federal offenders to reenter society. The report discussed such issues as inmate participation and marketable skills learned in rehabilitation programs, prerelease job-placement services, funding of vocational training programs, and program needs and progress. Appropriate recommendations were made to the Department of Justice regarding these issues.

## CHAPTER 2

### INDUSTRIAL OPERATIONS

Fiscal year 1973 sales to Government agencies totaled almost \$54 million, or about \$2.7 million more than in the preceding year. These sales resulted in profits of \$6.6 million, an increase of \$245,577 over profits of the previous year.

Industrial profits were distributed as follows: \$5.2 million, which includes depreciation expenses, was used to support the vocational training programs; and \$999,452 was spent on meritorious compensation to inmates and inmate accident compensation. Profits retained by the corporation amounted to \$384,039, a decrease of about \$11,000 from that of the preceding year.

Of the 52 industrial operations in effect during the year, 26 showed increases in sales volume from the preceding year totaling \$7.4 million. The largest increase, \$1.1 million, occurred at the canvas specialties factory in the Atlanta institution. During the year the corporation began five new industries. Of these industries, three had aggregate sales volume of \$1.4 million and profits of \$119,940. Two furniture-manufacturing industries which began at year-end had no sales activity.

During the fiscal year five industries (a clothing industry and four furniture-refinishing industries) were discontinued primarily because they were unprofitable operations. They had aggregate sales of \$1,149,599 and losses of \$335,614. Also during the year the sign factory at McNeil Island, Washington, was relocated to Lompoc, California, and the parachute industry at Atlanta, Georgia, was integrated with its canvas specialties industry.

### CASH AVAILABILITY

At June 30, 1973, the corporation's available cash of \$4.6 million represented a decrease of about 28 percent from the preceding year. Available cash further decreased to \$2.5 million in October 1973. Corporation officials advised us in October that they had initiated an immediate action plan to improve the declining cash position. We will continue to evaluate the corporation's cash position and actions



taken to improve it as a part of our annual review of operations.

CHANGE IN PERCENTAGE OF MARKUP  
ON INTERINDUSTRY INVENTORIES

The corporation manufactures a variety of products that are sold to Government agencies. Some of the items that are sold to Government agencies are also sold to industries within the corporation. These interindustry sales primarily consist of items purchased from one industry for incorporation into an end product by another industry. These end products are then sold to Government agencies.

The policy of the corporation, when selling items between industries, is to sell them at the same profit margin at which they are sold to Government agencies. The interindustry profit is subsequently eliminated from inventories at yearend. In the past this profit was eliminated by applying to these inventories a markup percentage computed by dividing the gross profit on interindustry transactions by total interindustry sales. In deriving the gross profit figure, certain cost factors, such as selling and administrative expenses, were excluded. These costs, however, were incurred on interindustry sales as well as on sales to Government agencies.

In order to show more accurate costs and profits for interindustry transactions, the corporation changed its procedures for eliminating the interindustry profit from inventories. Beginning with the fiscal year 1973 financial statements, the corporation is using a revised percentage computed by dividing the net industrial profit of the corporation by total sales, including interindustry sales. Thus the previously omitted cost factors are an integral part of the revised method of calculation.

The net monetary effect of this percentage change is approximately \$100,000 and affects all the corporation's financial statements. Had the corporation continued its use of the old method of profit elimination, total inventory, capital, and net industrial profit would have been about \$100,000 less than as reported on the fiscal year 1973 financial statements.

## CHAPTER 3

### SCOPE OF EXAMINATION

Our examination of the financial statements of the Federal Prison Industries, Inc., for fiscal year 1973 was made in accordance with generally accepted auditing standards and included such tests of the accounting records and financial transactions and such other auditing procedures as we considered necessary in view of the nature and volume of the transactions and the effectiveness of the internal controls, including the internal audit function.

The Office of Internal Audit, Department of Justice, reviewed fiscal year 1973 financial operations at 12 industrial locations and assisted us in reviewing the corporation's consolidated financial statements. We relied greatly on the work of the internal auditors when rendering an opinion on the financial statements.

We made our examination at the central office in Washington, D.C., and at the institutions in Alderson, West Virginia, and Atlanta, Georgia.

## CHAPTER 4

### OPINION ON FINANCIAL STATEMENTS

In our opinion, the accompanying financial statements (schs. 1, 2, and 3) present fairly the financial position of the Federal Prison Industries, Inc., at June 30, 1973, and the results of its operations and the changes in financial position for the year then ended, in conformity with principles and standards of accounting prescribed for executive agencies by the Comptroller General of the United States applied on a basis consistent with that of the preceding year--except for the change in the method for eliminating interindustry profit from inventories, with which we concur.

FINANCIAL STATEMENTS

FEDERAL PRISON INDUSTRIES, INC.

STATEMENT OF FINANCIAL CONDITION  
FISCAL YEARS ENDED JUNE 30, 1973 AND 1972

A S S E T S

	<u>Fiscal year 1973</u>	<u>Fiscal year 1972</u>
FUNDS WITH U.S. TREASURY:		
Available for operations	\$ 4,638,255	\$ 6,433,649
Special deposits	17,755	47,716
ACCOUNTS RECEIVABLE (principally from Government agencies)	7,004,877	5,883,911
INVENTORIES (at cost) (note 2):		
Materials and supplies	\$13,011,640	\$11,709,745
Work in process	4,150,166	3,704,113
Finished goods	<u>4,684,242</u>	<u>4,018,650</u>
Total inventories	21,846,048	19,432,508
PLANT AND EQUIPMENT (at cost or appraised value less depreciation):		
Machinery and equipment	10,851,521	11,134,749
Buildings and improvements	17,118,016	17,040,541
Construction in process	<u>2,072,908</u>	<u>1,878,907</u>
Total plant and equipment	30,042,445	30,054,197
SUNDRY ASSETS	<u>165,814</u>	<u>98,530</u>
Total assets	<u>\$63,715,194</u>	<u>\$61,950,511</u>

The notes on page 14 are an integral part of this statement.

## LIABILITIES AND CAPITAL

	<u>Fiscal year 1973</u>	<u>Fiscal year 1972</u>
LIABILITIES:		
Accounts payable	\$ 2,706,783	\$ 2,611,492
Accrued liabilities	1,837,669	1,210,244
Employees' accrued annual leave	1,172,488	1,083,744
Deposit fund liabilities	<u>17,755</u>	<u>47,716</u>
Total liabilities	<u>5,734,695</u>	<u>4,953,196</u>
CONTINGENT LIABILITIES	<u>-</u>	<u>25,687</u>
CAPITAL:		
Initial investment of U.S.		
Government	4,176,040	4,178,040
Property received from other		
Government agencies, net	3,156,887	2,562,365
Net income since inception (note 2)	\$132,647,572	\$132,233,223
Less dividends paid into U.S.		
Treasury	<u>82,000,000</u>	<u>82,000,000</u>
Retained earnings (note 3)	<u>50,647,572</u>	<u>50,233,223</u>
Total capital	<u>57,980,499</u>	<u>56,971,628</u>
Total liabilities and capital	<u>\$63,715,194</u>	<u>\$61,950,511</u>

SCHEDULE 2

FEDERAL PRISON INDUSTRIES, INC.

STATEMENT OF INCOME AND EXPENSE

FISCAL YEARS ENDED JUNE 30, 1973 AND 1972

	<u>Fiscal year 1973</u>		<u>Fiscal year 1972</u>	
Total sales of products and services	\$58,757,095		\$53,995,326	
Less sales between industries	<u>4,765,064</u>		<u>2,717,828</u>	
Sales to Government agencies	53,992,031		51,277,498	
Cost of goods and services sold	<u>44,614,249</u>		<u>42,527,523</u>	
Gross profit		<u>\$9,377,782</u>		<u>\$8,749,975</u>
OPERATING EXPENSES:				
Sales expenses:				
Outgoing freight	87,225		86,442	
Shipping	399,349		331,919	
Catalog, samples, and sundries	<u>18,950</u>	505,524	<u>56,716</u>	475,077
Administrative expenses:				
Salaries and related	919,229		792,023	
Travel	80,202		74,806	
General Accounting Office audit	25,000		25,000	
Department of Justice audit	125,000		97,000	
Rent for Washington office	30,553		27,160	
Telephone	46,814		28,221	
Printing and reproduction	26,448		21,389	
Building repairs	11,590		21,866	
Freight	24,735		12,739	
Reimbursable salaries (con-			35,404	
struction)	<u>58,584</u>		<u>19,264</u>	
Other				
Total administrative expenses				
subject to limitation set				
by the Congress (1972--		1,348,155		1,154,872
\$1,164,000) (1973--				
\$1,500,000)				
Depreciation:				
Machinery and equipment	3,904		3,074	
Building and improvements	<u>-</u>	<u>3,904</u>	<u>1,511</u>	<u>4,585</u>
NET OPERATING EXPENSES		1,857,583		1,634,534
OTHER INCOME:				
Miscellaneous sales income	152,400		211,837	
Sundry income	<u>52,875</u>	205,275	<u>64,996</u>	276,833
OTHER EXPENSES:				
Survey of inventory	171,774		119,130	
Reimbursable salaries and related	649,388		636,819	
Loss on disposition of assets	87,513		101,695	
Christmas packages to inmates	29,820		28,400	
Factory closing and organization				
expense	29,079		42,591	
Other expense	138,024		92,770	
Incentive awards to civilians	<u>9,725</u>	<u>1,115,323</u>	<u>6,295</u>	<u>1,027,700</u>
NET INDUSTRIAL PROFIT		6,610,151		6,364,574
Less:				
Accident compensation	98,504		125,101	
Vocational expense	5,226,660		5,074,182	
Meritorious compensation to				
inmates	<u>900,948</u>	<u>6,226,112</u>	<u>770,243</u>	<u>5,969,526</u>
NET PROFIT TO RETAINED INCOME (note 2)		<u>\$ 384,039</u>		<u>\$ 395,048</u>

The notes on page 14 are an integral part of this statement.

## FEDERAL PRISON INDUSTRIES, INC.

## STATEMENT OF CHANGES IN FINANCIAL POSITION

FISCAL YEAR ENDED JUNE 30, 1973

FUNDS PROVIDED:		
Sales of products and services		\$53,992,031
Miscellaneous sales		2,904,040
Materials and supplies received without exchange of funds		565,415
Sundry income current year		52,875
Sundry income earned in prior years		<u>156,634</u>
Total funds provided		<u>\$57,670,995</u>
FUNDS APPLIED:		
Cost of goods and services sold	\$44,614,249	
Less production depreciation	<u>1,664,360</u>	\$42,949,889
Vocational training and placement expense	5,226,660	
Less depreciation	<u>484,046</u>	4,742,614
Administrative expense	1,352,059	
Less depreciation	<u>3,904</u>	1,348,155
Acquisition of fixed assets		2,111,451
Cost of miscellaneous sales		2,751,640
Other operating expense		1,533,334
Inmate compensation for meritorious or outstanding service		900,948
Accident compensation		98,504
Loss on disposal of assets		87,513
Operating expenses incurred in prior years		126,324
Increase in working capital		<u>1,020,623</u>
Total funds applied		<u>\$57,670,995</u>

The notes on page 14 are an integral part of this statement.



## NOTES TO FINANCIAL STATEMENTS

1. Accounting policies
  - a. The consolidated financial statements include the accounts of the central office of the Federal Prison Industries, Inc., and its industrial facilities. Appropriate eliminations are made for interindustry transactions and profits therefrom.
  - b. Federal Prison Industries, Inc., uses the straight-line method of depreciation for all depreciable assets. Rates of depreciation are based on useful life guidelines established in Revenue Procedures 6221, issued by the U.S. Treasury Department, Internal Revenue Service.
  - c. Raw materials inventory is recorded at actual cost.
  - d. Work in process and finished goods inventories are recorded at actual cost determined by one of the following cost systems: process costing, job costing, or standard costing, depending upon the type of industry.
2. Beginning with fiscal year 1973 the corporation revised its procedures for eliminating interindustry profit from inventories. The percentage for eliminating interindustry profit is based on the relationship between net industrial profit and total sales. Before fiscal year 1973 the percentage was based on the relationship between interindustry gross profit and sales. Had the corporation continued to use the previous method, the inventory, capital, and net industrial profit would have been about \$100,000 less than as shown in the financial statements.
3. Inclusive of \$30,310 representing adjustments affecting prior years' transactions.

APPENDIX

PRINCIPAL OFFICIALS OF  
FEDERAL PRISON INDUSTRIES, INC.

	<u>Date appointed</u>	<u>Representatives of</u>
BOARD OF DIRECTORS:		
James L. Palmer, President	Sept. 1951	Retailers and consumers
John Marshall Briley, Vice President	Jan. 1960	Secretary of Defense
George Meany	Dec. 1947	Labor
Berry N. Beaman	Jan. 1954	Industry
William E. Morgan	May 1966	Agriculture
Vacant	-	Attorney General

## COMMISSIONER OF INDUSTRIES:

Norman A. Carlson

ASSOCIATE COMMISSIONER OF  
INDUSTRIES:

Loy S. Hayes

## SECRETARY:

Paul Plein

ASSISTANT COMMISSIONER FOR  
FINANCIAL MANAGEMENT:

A. I. McAlear

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