DEPARTMENT OF JUSTICE
FEDERAL BUREAU OF PRISONS

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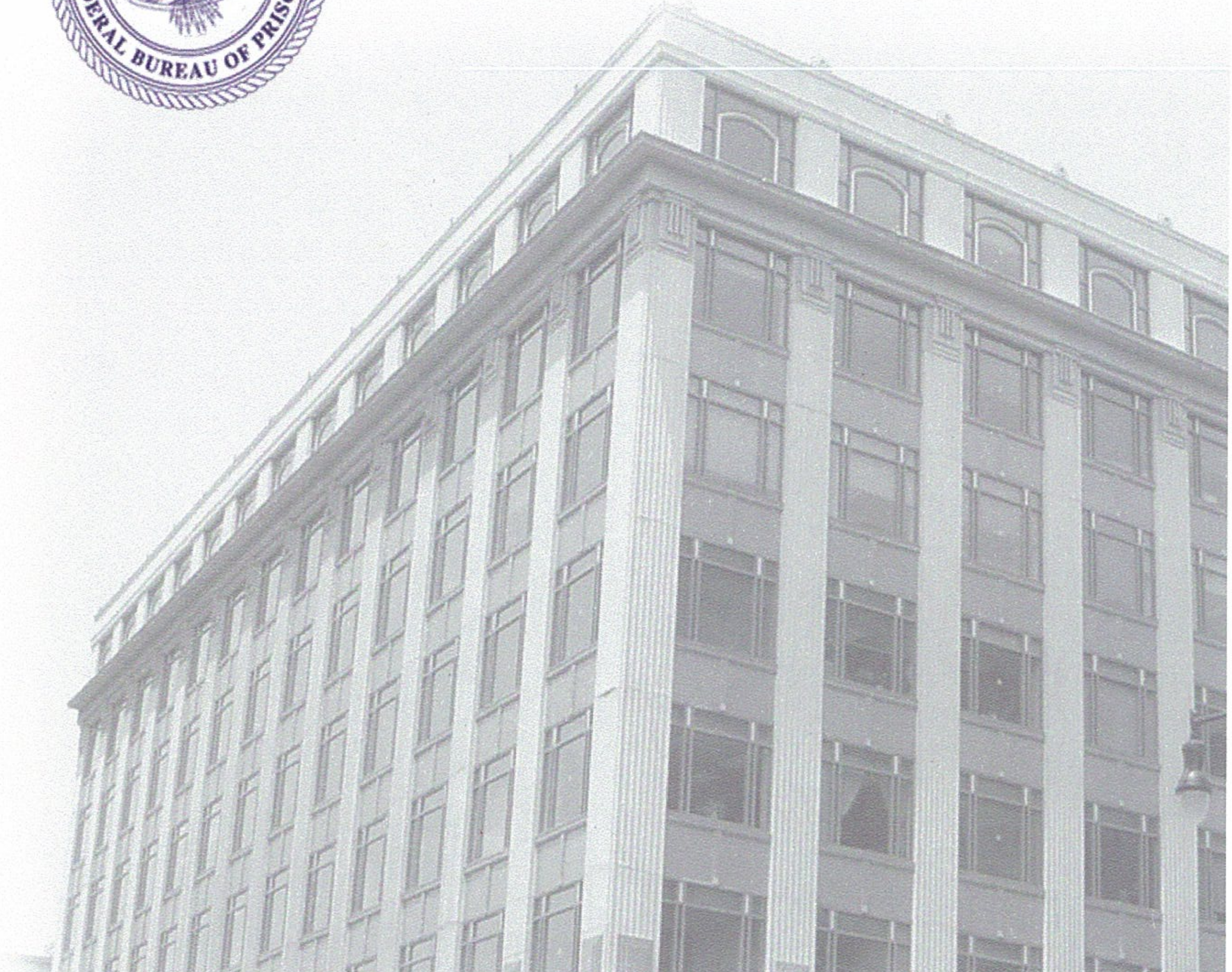

FEDERAL PRISON INDUSTRIES, INC.
Fiscal Year 2013
Annual Management Report
December 16, 2013

We are pleased to present the Federal Prison Industries, Inc.'s (FPI) Fiscal Year 2013 Annual Management Report to the Congress of the United States. This report includes the FPI's financial statements, Management's Discussion and Analysis, Office of the Inspector General Commentary and Summary, and the independent auditors' reports on the Corporation's financial statements, internal controls over financial reporting and compliance and other matters. FPI's financial statements received an unmodified audit opinion and no significant deficiencies or material weaknesses were reported.

FPI was established by statute and Executive Order 6917 in 1934, signed by President Roosevelt to provide opportunities for educational and work-related experiences to federal offenders. Although a great deal of time has passed and technology is changing rapidly, FPI's mission throughout the past 79 years remains the same -- to protect society and reduce crime by preparing inmates for successful reentry through job training.

As the Bureau of Prisons' (BOP's) most important inmate reentry program, approximately 13,000 federal inmates were working in FPI factories at fiscal year-end. The need to address inmate idleness was a contributing factor in the creation of FPI in 1934. This program continues to directly support the BOP's mission by keeping inmates productively occupied which lowers the likelihood that they will engage in disruptive behavior and contributes significantly to the safe and secure management of prisons. Additionally, inmates participating in the FPI program have an increased likelihood of successful reentry into society and are significantly less likely to return to a life of crime, which reduces future costs of enforcement and incarceration.

FPI is a program with proven lasting benefits, including reduced recidivism; a positive impact on the U.S. economy through the raw materials purchased from suppliers around the country, and the staff salaries spent in the community, all without an additional tax burden to society.

As a federal government corporation, FPI is a program that also functions as a business to remain self-sustaining, and continues to face a dynamic set of external and internal constraints. Due to the nature of the changes affecting purchases from FPI by the government sector, emphasis has been placed on exploring more opportunities with commercial customers. New market authorities, contained in the Consolidated and Further Continuing Appropriations Act of 2012 (P.L. 112-55) are now available for FPI to obtain commercial customers through repatriation and bringing sales otherwise sent to foreign countries back into the United States. Many new opportunities are being pursued and a number of pilot programs have already been implemented which allowed several hundred inmates to participate in repatriated work projects during this fiscal year. Additionally, FPI is now authorized to participate in the Prison Industries Enhancement Certification Program (PIECP). FPI obtained approval of its PIECP application from the Bureau of Justice Assistance on May 31, 2013. FPI has pursued this opportunity in fiscal year 2013 through research and discussions with successful state agencies, and plans to move forward with implementation of the program in fiscal year 2014.

FPI is thankful for the support from all of the Department of Justice agencies in assisting with the development of work opportunities to support our mission. Thanks to the outstanding contributions and dedication of FPI staff as well as the exceptional leadership provided by the Board of Directors, FPI will continue to fulfill its mission and continue to concentrate its efforts on opportunities that will allow it to succeed in the years ahead.

Charles E. Samuels, Jr.	Mary M. Mitchell
Chief Executive Officer	Chief Operating Officer

U.S. Department of Justice
Federal Prison Industries, Inc.
Management's Discussion and Analysis
(Unaudited)

Mission

It is the mission of Federal Prison Industries, Inc. (FPI) to protect society and reduce crime by preparing inmates for successful reentry through job training.

Organizational Structure of Federal Prison Industries, Inc.

FPI is a wholly-owned government corporation created by Congress in 1934. FPI is authorized to operate industries in federal penal and correctional institutions and disciplinary barracks (18 U.S.C. § 4121 to § 4129). The Director of the Federal Bureau of Prisons (BOP), who has jurisdiction over all federal correctional institutions, is the Chief Executive Officer. General management of FPI is provided by the Chief Operating Officer who also serves as an Assistant Director for the BOP.

In fiscal year 2013, FPI operated in five business segments: Clothing and Textiles, Electronics, Office Furniture, Recycling, and Services. FPI has industrial and service operations at 78 factories located at 62 prison facilities as of September 30, 2013. Factories are operated by FPI supervisors and managers, who train and oversee the work of inmates. The factories utilize raw material and component parts purchased from the private sector to produce finished goods. Orders for goods and services are obtained through marketing and sales efforts managed by FPI staff. Some products and all services are provided on a non-mandatory, preferred source basis.

FPI processes primarily all customer orders and billings along with vendor payments through a centralized service center at Lexington, Kentucky.

Financial Structure

FPI operates as a revolving fund and does not receive an annual appropriation. The majority of revenues are derived from the sale of products and services to other federal departments, agencies, and bureaus. Operating expenses such as the cost of raw materials and supplies, inmate wages, staff salaries, and capital expenditures are applied against these revenues resulting in operating income or loss, which is reapplied toward operating costs for future production. In this regard, FPI makes capital investments in buildings and improvements, machinery, and equipment as necessary in the conduct of its industrial operation.

FPI sells products and services to the majority of federal departments, agencies and bureaus. FPI's largest federal government customers include the Department of Defense (DOD), the Department of Homeland Security (DHS), the Department of Justice (DOJ), the General Services Administration (GSA), and the Social Security Administration (SSA).

Due to the nature of the changes effecting Federal Prison Industries with the government sector, emphasis has been placed on exploring more opportunities with commercial customers. Opportunities in this arena have become available as part of the approval for FPI to obtain commercial customers through repatriation and bringing sales otherwise sent to foreign countries back into the United States of America. Many new opportunities are already being pursued through a collaboration of FPI's business groups sections and the New Business Development Group. Additionally, the Consolidated and Further Continuing Appropriations Act of 2012 (P.L. 112-55) authorized FPI to participate in the Prison Industries Enhancement Certification Program (PIECP). FPI has invested significant time and effort into pursuing this goal in fiscal year 2013 through research and discussion within our organization and other agencies. FPI obtained approval of its PIECP application from the Bureau of Justice Assistance in May 2013. FPI will continue to aggressively pursue the implementation of the PIECP program in fiscal year 2014.

Critical Accounting Policies

The following discussion and analysis of FPI's financial condition, results of operations, liquidity and capital resources are based upon FPI's financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles based on accounting standards issued by the Financial Accounting Standards Board (FASB), the private sector standards-setting body. These generally accepted accounting principles require FPI management to make estimates and judgments that affect the reported amount of assets, liabilities, revenues and expenses. In this regard, FPI management evaluates the estimates on an on-going basis, including those related to product returns, bad debt, inventories, long-lived assets, and contingencies and litigation. FPI bases its estimates upon historical experience and various other assumptions that FPI believes are reasonable under the circumstances. The actual results may differ from these estimates when assumptions or conditions change.

FPI believes that some of its accounting policies involve complex or higher degrees of judgment than its other accounting policies. The following accounting policies have been identified by FPI management as being critical and therefore require more significant estimates or reliance on a higher degree of judgment on the part of FPI management.

Revenue recognition: Revenue is generally recognized when 1) delivery has occurred or services have been rendered, 2) persuasive evidence of an arrangement exists, 3) there is a fixed or determinable price, and 4) collectability is reasonably assured. Revenue from contracts that specify a customer acceptance criteria is not recognized until either customer acceptance is obtained or upon completion of the contract. Sales returns are primarily replaced with like items and are recorded as they occur.

Revenue is recognized on multiple element (numerous stages of product delivery, set up, and installation) agreements as a single unit of accounting for manufactured items when the product has been accepted by the customer. Revenue for services provided on behalf of FPI is recognized when the service provider presents a valid invoice including a customer acceptance or completion notice.

Allowance for doubtful accounts receivable: The allowance for doubtful accounts is based upon an analysis of several factors including payment trends, historical write off experience, credit quality for non-governmental accounts, and specific analysis of collectability of an account. During the course of time, these factors may change which will cause the allowance level to adjust accordingly. As part of their analysis, customer accounts determined to be unlikely to be paid are recorded as a charge to bad debt expense in the income statement and the allowance account is increased. When it becomes certain that a customer account will not be paid, the receivable is written off by removing the balance from accounts receivable.

As of September 30, 2013 and September 30, 2012, FPI had established an allowance for bad debt in the amount of $.41 million and $.52 million on accounts receivable balances of $39.49 million and $26.66 million, respectively.

Inventory valuation: FPI maintains its inventory primarily for the manufacture of goods for sale to its customers. FPI's inventory is composed of three categories: Raw Materials, Work-in-Process, and Finished Goods. These categories are generally defined by FPI as follows: Raw Materials consist of materials that have been acquired and are available for the production cycle, Work-in-Process is composed of materials that have moved into the production process and have some measurable amount of labor and overhead added by FPI, Finished Goods are materials with FPI added labor and overhead that have completed the production cycle and are awaiting sale to customers.

Raw material inventory value is based upon moving average cost. Inventories are valued at the lower of average cost or market value (LCM) and include materials, labor and manufacturing overhead. Market value is calculated on the basis of the contractual or anticipated selling price, less allowance for administrative expenses. FPI values its finished goods and sub-assembly items at a standard cost that is periodically adjusted to approximate actual cost. FPI has established inventory allowances to account for LCM adjustments and obsolete items that may not be utilized in future periods.

Program Values

It is FPI's vision to protect society, reduce crime, aid in the security of the nation's prisons and decrease taxpayer burden, by assisting inmates with developing vital skills necessary for successful re-entry into society. Through the production of market-priced quality goods and services, FPI provides job training and work opportunities to inmates, while minimizing impact on private industry and labor.

The goal of FPI is to reduce undesirable inmate idleness by providing a full-time work program for inmate populations. Many of the inmates do not have marketable employment skills. FPI provides a program of constructive industrial work and services wherein job skills can be developed and work habits acquired.

FPI has existed as an effective correctional program for 79 years. Over the course of these years, FPI has positively impacted countless staff and inmate lives. In the face of an escalating inmate population and an increasing percentage of inmates with histories of violence, FPI's programs have helped ease tension and avert dangerous situations, thereby protecting lives and federal property. FPI work programs provide meaningful activities for inmates, thereby playing an essential role in the operation of safe, secure and less costly prisons.

At the same time, FPI provides opportunities for inmates who want to take the personal responsibility for rehabilitating themselves. More than 95 percent of inmates eventually will be returned to society; industrial programs can help them to steer clear of criminal activity after release. Participation in FPI programs improves the likelihood that inmates will remain crime-free upon their release from BOP custody. A comprehensive study conducted by the BOP demonstrated that FPI provides inmates with an opportunity to develop work ethics and skills, contributes substantially to lower recidivism and increases job-related success of inmates upon release. This study indicates that inmates involved in FPI work programs are substantially less likely to return to prison. The impact on the lives of people who live in the communities in which these inmates will return is immeasurable. Countless lives are spared the devastating impact of continued criminal activity.

Analysis of Financial Statements

Cash and Investments

Cash and Cash Equivalents decreased $18.4 million during the year. An increase in Accounts Receivable of $12.9 million contributed to a reduction of FPI (non-advance) cash of $11.6 million during fiscal year 2013. Cash Advances decreased by $6.9 million. FPI's cash advances are primarily for the purchase of inventory in support of the Fleet Management and Vehicular Components vehicle retrofitting operation. The primary customer for these operations is the Department of Homeland Security; advances fluctuate throughout the year as they receive appropriations.

Accounts Receivable

The Accounts Receivable balance increased $12.9 million during fiscal year 2013. The Accounts Receivable balance of $39.1 million as of September 30, 2013, represents 78.6 percent of September's total revenues. FPI's average days to collect for fiscal year 2013 was approximately 24. The Accounts Receivable balance over sixty days old represented 7.8 percent of the total balance as of September 30, 2013.

Inventory

Inventory decreased by $33.8 million during fiscal year 2013. FPI continued to place emphasis on inventory reduction during fiscal year 2013. The Electronics business segment was the primary contributor to the reduction with a decrease of $33.1 million. The Electronics segment decrease can be attributed to the decrease in fleet vehicle, solar panel and cable product line inventories totaling $24.8 million, $5.8 million and $3.0 million respectively.

Liabilities

Total Liabilities decreased by $42.4 million during fiscal year 2013. The primary contributors to the decrease were a $35.8 million reduction in Advances Payable and a $3.5 million reduction in Accounts Payable. This decrease is attributable to a change in customer advances payable on hand primarily for the retrofitting of vehicles for the Department of Homeland Security (DHS) as a result of a decrease in customer contracts. The decrease in Accounts Payable is relative to a corresponding reduction in inventory as a result of an overall decrease in sales orders.

Revenue, Cost of Revenue and Net Loss

Total Revenue decreased by $88.4 million while total cost of revenue decreased by $94.1 million. The decrease in revenue resulted primarily from the decrease in sales revenue of $72.8 million and a reduction in corresponding freight collections of $7.3 million. The largest business segments showing a decrease in sales were Electronics $49.3 million, Office Furniture with $42.3 million, and Services with $4.6 million. The Textiles and Recycling business segments had offsetting increases of $21.2 million and $2.3 million in sales respectively. The Net Loss decreased $24.0 million in fiscal year 2013 compared to fiscal year 2012. Factory Earnings were $14.5 million higher in fiscal year 2013 than the previous fiscal year primarily due to a reduction in factory overhead of $11.0 million.

Business Segments

In fiscal year 2013, FPI's businesses were organized, managed and internally reported as five operating segments based on products and services. These segments are Clothing and Textiles, Electronics, Office Furniture, Recycling, and Services. FPI is not dependent on any single product as a primary revenue source; however, it is currently primarily dependent on the federal government market for the sale of its products. FPI's net industrial income (earnings) at the business segment level consists of sales offset by cost of goods sold and under /over applied overhead. FPI redefined its business segments from six categories to five in fiscal year 2013. The Fleet and Industrial Products business segment was consolidated into the Electronics, Office Furniture, and Services business segments. As a result, net sales and earnings for fiscal year 2012 for Electronics, Office Furniture, and Services have been reclassified for comparative purposes.

Business Segment	Fiscal Year	
Clothing and Textiles	**2013**	**2012**
Sales	$235,691	$214,522
Earnings	$36,663	$20,642
Electronics		
Sales	$128,120	$177,462
Earnings	($3,969)	($8,964)
Office Furniture		
Sales	$118,533	$160,850
Earnings	$3,904	$12,350
Recycling		
Sales	$17,900	$15,563
Earnings	$6,566	$4,764
Services		
Sales	$33,093	$37,717
Earnings	$3,051	$2,921
Corporate Total		
Sales	$533,337	$606,114
Earnings	$46,215	$31,713

Possible Future Effects of Existing Events and Conditions

During fiscal year 2013, FPI encountered a decline in sales for the fourth consecutive year and experienced a net loss for the fifth consecutive year. Although sales revenue continued to decline by $72.8 million during fiscal year 2013, the net loss of $4.3 million was a considerable improvement when compared to the fiscal year 2012 loss of $28 million. The $4.3 million loss is not as substantial as would be expected considering the rate of decline in sales. This variation can be attributed to on-going cost containment initiatives by FPI. Included in this net loss is approximately $3.9 million in write down of solar panel inventory.

In fiscal years 2014 and beyond, FPI faces the additional challenge of the shrinking federal budget, the resulting decline in discretionary spending and the ultimate impact of decline in FPI sales. FPI continues to make every effort to mitigate the impact of these challenges through aggressively pursuing new customers and new products, employment of part time inmates, staffing and other cost reductions, new opportunities for revenue, and stringent measures to control cash. Additionally, FPI has been active in communicating with our federal customers to determine if our current product offerings meet their current needs and to make them aware of new repatriated product offerings. Further emphasis has been placed on DOJ agencies through meetings with component heads and tracking of their respective incoming orders. Due to the collective impact of these efforts, FPI's operating plan for fiscal year 2014 projects a $38 thousand net income.

Prison Industries Enhancement Certification Program

The Consolidated and Further Continuing Appropriations Act of 2012 (P.L. 112-55) authorized FPI to participate in the Prison Industries Enhancement Certification Program (PIECP) and to manufacture products that would otherwise be produced outside of the United States, as approved by FPI's Board of Directors. FPI has invested significant time and effort into pursuing this goal in fiscal year 2013 through research and discussion within our organization and other agencies. FPI obtained approval of its PIECP application from the Bureau of Justice Assistance in May 2013. FPI will continue to aggressively pursue the implementation of the PIECP program in fiscal year 2014.

Repatriation

Due to the nature of the changes effecting Federal Prison Industries with the government sector, emphasis has been placed on exploring more opportunities with commercial customers. Opportunities in this arena have become available as part of the approval for FPI to obtain commercial customers through repatriation and bringing sales otherwise sent to foreign countries back into the United States of America. Many new opportunities are already being pursued through a collaboration of FPI's business group sections and the New Business Development Group.

Part Time Inmates

FPI's continued emphasis on the use of part time and half time inmate workers resulted in a 41 percent increase during fiscal year 2013, adding 728 inmates to the classification, which contributed significantly to FPI meeting its goal to employ 13,000 inmates during 2013. Continued emphasis in 2014 and beyond will allow for an increase in the number of inmates participating in the FPI program while reducing the per inmate cost of employment. Concentration on this goal will increase the impact on the number of inmates released with FPI experience.

Long Term Investment

During fiscal year 2013, FPI began investing in long-term market bonds through the Treasury Department. Past research revealed that it was not advantageous. Due to changed rates and market conditions, the prospect of investing in long term bonds was re-evaluated and was determined to be beneficial to pursue. The initial investment into the bonds occurred in January 2013 and an additional amount was invested later in the fiscal year. Due to the long-term nature of the bonds, FPI receives a higher rate of return on their investment of cash in these bonds. As a result, fiscal year 2013 investment earnings are approximately twice what they would have been had the long-term option not been pursued.

Payment Card

During fiscal year 2013, FPI evaluated the benefit that may be derived from implementing the J.P. Morgan bank card as a payment card. It was determined that the potential exists for substantial income to be generated through rebates. FPI is in the process of implementing this program with the first significant benefits to be received in January 2014. The operating plan for 2014 includes an estimate of $3 million dollars additional income to be generated from this program.

Pending Investigations

In December 2009, the Department of Justice, Office of the Inspector General, initiated an investigation regarding the manufacturing and quality procedures for some of the military helmets produced by FPI. This investigation is still ongoing. FPI's management is committed to ensuring FPI produces a quality product that meets the requirements of our customers.

FEDERAL PRISON INDUSTRIES, INC.
ANNUAL FINANCIAL STATEMENTS
FISCAL YEAR 2013

OFFICE OF THE INSPECTOR GENERAL
COMMENTARY AND SUMMARY

This audit report contains the Annual Financial Statements of the Federal Prison Industries, Inc. (FPI) for the fiscal years (FY) ended September 30, 2013, and September 30, 2012. In accordance with the Government Corporation Control Act, as amended (31 U.S.C. §9105), and under the direction of the Office of the Inspector General (OIG), KPMG LLP performed the FPI's audit in accordance with auditing standards generally accepted in the United States of America. Effective for FY 2013, auditing standards generally accepted in the United States of America use the term "unmodified" opinion instead of "unqualified" opinion. The definition of the two terms is substantially the same. An unmodified opinion means that the financial statements are presented fairly, in all material respects, in accordance with U.S. generally accepted accounting principles. The FY 2013 audit resulted in an unmodified opinion on the FY 2013 financial statements. The FY 2012 financial statements audit was performed by Cotton & Company LLP and resulted in an unqualified opinion (OIG Audit Report No. 13-03).

KPMG LLP also issued reports on internal control over financial reporting and on compliance and other matters. The auditors did not identify any material weaknesses, nor did they report any significant deficiencies in the FY 2013 *Independent Auditors' Report on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards.* No instances of non-compliance or other matters that are required to be reported under *Government Auditing Standards* were identified during the audit in the FY 2013 *Independent Auditors' Report on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards*. Additionally, KPMG LLP's tests disclosed no instances in which the FPI's financial management systems did not substantially comply with the *Federal Financial Management Improvement Act of 1996*.

The OIG reviewed KPMG LLP's reports and related documentation and made necessary inquiries of its representatives. Our review, as differentiated from an audit in accordance with *Government Auditing Standards*, was not intended to enable us to express, and we do not express, an opinion on the FPI's financial statements, conclusions about the effectiveness of internal control, conclusions on whether the FPI's financial management systems substantially complied with the *Federal Financial Management Improvement Act of 1996*, or conclusions on compliance with laws and regulations and other matters. KPMG LLP is responsible for the attached auditors' reports dated December 3, 2013, and the conclusions expressed in the reports. However, our review disclosed no instances where KPMG LLP did not comply, in all material respects, with auditing standards generally accepted in the United States of America.

KPMG LLP
Suite 12000
1801 K Street, NW
Washington, DC 20006

Independent Auditors' Report on the Financial Statements

Inspector General
U.S. Department of Justice

Chief Executive Officer
Board of Directors
Federal Prison Industries, Inc.
U.S. Department of Justice

We have audited the accompanying financial statements of the U.S. Department of Justice Federal Prison Industries, Inc. (FPI) which comprise the balance sheet as of September 30, 2013, and the related statements of operations and cumulative results of operations, and cash flows (hereinafter referred to as "financial statements") for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 14-02, *Audit Requirements for Federal Financial Statements*. Those standards and OMB Bulletin No. 14-02 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion on the Financial Statements

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the U.S. Department of Justice Federal Prison Industries, Inc. as of September 30, 2013, and its net loss, cumulative results of operations, and cash flows for the year then ended in accordance with U.S. generally accepted accounting principles.

Other Matters

Prior Period Financial Statements Audited by a Predecessor Auditor

The accompanying financial statements of the FPI as of September 30, 2012 and for the year then ended were audited by other auditors whose report thereon dated November 5, 2012, expressed an unmodified opinion on those financial statements.

Other Information

Our audit was conducted for the purpose of forming an opinion on the basic financial statements as a whole. The Management Discussion and Analysis is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our fiscal year 2013 report dated December 3, 2013 on our consideration of the FPI's internal control over financial reporting, and our fiscal year 2013 report dated December 3, 2013 on our tests of its compliance with certain provisions of laws, regulations, contracts, and other matters. The purpose of those reports is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the FPI's internal control over financial reporting and compliance.

KPMG LLP

December 3, 2013

KPMG LLP
Suite 12000
1801 K Street, NW
Washington, DC 20006

Independent Auditors' Report on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Inspector General
U.S. Department of Justice

Chief Executive Officer
Board of Directors
Federal Prison Industries, Inc.
U.S. Department of Justice

We have audited, in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 14-02, *Audit Requirements for Federal Financial Statements*, the financial statements of the U.S. Department of Justice Federal Prison Industries, Inc. (FPI), which comprise the balance sheet as of September 30, 2013, and the related statements of operations and cumulative results of operations, and cash flows (hereinafter referred to as "financial statements") for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated December 3, 2013.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements as of and for the year ended September 30, 2013, we considered the FPI's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the FPI's internal control. Accordingly, we do not express an opinion on the effectiveness of the FPI's internal control. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and the results of that testing, and not to provide an opinion on the effectiveness of the FPI's internal control. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the FPI's internal control. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

December 3, 2013

KPMG LLP
Suite 12000
1801 K Street, NW
Washington, DC 20006

Independent Auditors' Report on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Inspector General
U.S. Department of Justice

Chief Executive Officer
Board of Directors
Federal Prison Industries, Inc.
U.S. Department of Justice

We have audited, in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 14-02, *Audit Requirements for Federal Financial Statements*, the financial statements of the U.S. Department of Justice Federal Prison Industries, Inc. (FPI), which comprise the balance sheet as of September 30, 2013, and the related statements of operations and cumulative results of operations, and cash flows (hereinafter referred to as "financial statements") for the year then ended and the related notes to the financial statements, and have issued our report thereon dated December 3, 2013.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the FPI's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 14-02. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests of compliance disclosed no instances of noncompliance or other matters that are required to be reported herein under *Government Auditing Standards* or OMB Bulletin No. 14-02.

We also performed tests of its compliance with certain provisions referred to in Section 803(a) of the *Federal Financial Management Improvement Act of 1996* (FFMIA). Providing an opinion on compliance with FFMIA was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests of FFMIA disclosed no instances in which the FPI's financial management systems did not substantially comply with the (1) federal financial management system requirements, (2) applicable federal accounting standards, and (3) application of the United States Government Standard General Ledger at the transaction level.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion on the FPI's compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the FPI's compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

December 3, 2013

Federal Prison Industries, Inc.

Balance Sheets

As of September 30, ***(DOLLARS IN THOUSANDS)***		**2013**		**2012**
Assets				
Current:				
Cash and cash equivalents	$	282,165	$	300,544
Accounts receivable, net		39,074		26,141
Inventories, net		95,411		129,254
Other assets		325		828
Total current assets		416,975		456,767
Property, plant and equipment, net		80,748		87,631
Total Assets	$	497,723	$	544,398
Liabilities and United States Government Equity				
Current:				
Accounts payable	$	38,295	$	43,595
Deferred revenue		59,098		94,892
Accrued salaries and wages		4,563		9,610
Accrued annual leave		7,337		8,133
Other accrued expenses		9,193		7,474
Total current liabilities		118,486		163,704
FECA actuarial liability		21,715		18,920
Total Liabilities		140,201		182,624
United States Government Equity				
Initial capital		4,176		4,176
Cumulative results of operations		353,346		357,598
Total United States Government Equity		357,522		361,774
Total Liabilities and United States Government Equity	$	497,723	$	544,398

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

Federal Prison Industries, Inc.

Statements of Operations and Cumulative Results of Operations

For the fiscal years ended September 30, ***(DOLLARS IN THOUSANDS)***	**2013**	**2012**
Revenue:		
Net sales	$ 533,337	$ 606,114
Other revenue	76,391	92,043
Total revenue	609,728	698,157
Cost of revenue:		
Cost of sales	486,494	566,410
Cost of other revenue	74,561	88,756
Total cost of revenue	561,055	655,166
Gross profit	48,673	42,991
Operating expenses:		
Sales and marketing	4,257	5,916
General and administrative	82,210	101,938
Total operating expenses	86,467	107,854
Loss from operations	(37,794)	(64,863)
Interest income	238	138
Interest expense	(2)	(1)
Other income, net	33,306	36,476
Net loss	(4,252)	(28,250)
Cumulative results of operations, beginning of fiscal year	357,598	385,848
Cumulative results of operations, end of fiscal year	$ 353,346	$ 357,598

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

Federal Prison Industries, Inc.

Statements of Cash Flows

For the fiscal years ended September 30, *(DOLLARS IN THOUSANDS)*	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	$ (4,252)	$ (28,250)
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	8,650	10,067
Loss on disposal of property, plant and equipment	291	7,549
Changes in:		
Accounts receivable	(12,933)	20,539
Inventories	33,843	4,680
Other assets	503	1,755
Accounts payable and accrued expenses	(6,629)	(56)
Deferred revenue	(35,794)	(4,777)
Net cash provided by (used in) operating activities	(16,321)	11,507
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property, plant and equipment	(2,058)	(2,384)
Construction-in-progress of plant facilities	-	(89)
Net cash used in investing activities	(2,058)	(2,473)
Net increase (decrease) in cash and cash equivalents	(18,379)	9,034
Cash and cash equivalents, beginning of fiscal year	300,544	291,510
Cash and cash equivalents, end of fiscal year	$ 282,165	$ 300,544

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

Fiscal Years 2013 and 2012
Notes to Financial Statements
(Dollars in Thousands)

Note 1. Organization and Mission

Federal Prison Industries, Inc. (FPI) was established in 1934 by an act of the United States Congress. FPI operates under the trade name UNICOR, as a wholly-owned federal government corporation within the Department of Justice, and functions under the direction and control of a Board of Directors, (the "Board"). Members of the Board are appointed by the President of the United States of America and represent retailers and consumers, agriculture, industry, labor, the Attorney General, and the Secretary of Defense. FPI's statutory mandate is to provide employment and training for inmates in the Federal Prison System while remaining self-sufficient through the sale of its products and services.

FPI's federal government customers include departments (percent of Revenue shown in parenthesis), agencies and bureaus such as the Department of Defense (59%), the Department of Homeland Security (12%), the Department of Justice (10%), the General Services Administration (6%), and the Social Security Administration (2%). These and other federal organizations are generally required to purchase products from FPI, if its products meet the customer's price, quality, and delivery standards, under a mandatory source preference specified in FPI's enabling statute and the Federal Acquisition Regulation.

FPI has industrial and service operations at 78 and 81 factories located at 62 and 63 prison facilities that employed 13,001 and 13,369 inmates representing approximately 7% and 8% of the work eligible inmate population as of September 30, 2013 and September 30, 2012, respectively.

Note 2. Summary of Significant Accounting Policies

Basis of Accounting

FPI transactions are recorded on the accrual basis of accounting. Under the accrual basis, revenues are recorded when earned and expenses are recorded when incurred, regardless of when the cash is exchanged.

Basis of Presentation

FPI has historically prepared its external financial statements in conformity with U.S. generally accepted accounting principles based on accounting standards issued by the Financial Accounting Standards Board (FASB), the private sector standards-setting body. The Federal Accounting Standards Advisory Board (FASAB) has been designated as the standards-setting body for federal financial reporting entities with respect to the establishment of US GAAP. FASAB allows certain government agencies to utilize FASB standards for Financial Statement presentations.

Use of Estimates

The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and contingent liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates.

Cash and Cash Equivalents

FPI considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. FPI's investment activities and cash equivalents include both overnight repurchase agreements and one-year market bonds with the Bureau of Public Debt of the United States Treasury. FPI's investment in market bonds is redeemable at any time without penalty at the original market interest rate and is therefore not subject to interest rate risk. As a result, these market bonds are classified as cash equivalents on the accompanying balance sheets. The market value of overnight purchase agreements is equivalent to cost. The discount on the market bonds is amortized monthly and recorded as investment income.

Accounts Receivable / Concentration of Credit Risk

Financial instruments that potentially subject FPI to concentrations of credit risk consist primarily of accounts receivable. FPI sells products and services to various federal government departments, agencies and bureaus, as well as certain private sector companies, without requiring collateral. Accounts receivable consists of amounts due from those entities and is stated net of an allowance for doubtful accounts.

FPI routinely assesses the payment histories of its federal customers and the financial strength of its private sector customers and maintains allowances for anticipated losses as they become evident. In this regard, an insignificant amount of accounts receivable remained past due at September 30, 2013 and September 30, 2012. A significant portion of these past due items relate to billings to various entities within Department of Defense (DOD) who rely on the Defense Finance and Accounting Service (DFAS) to process vendor payments. Historically, customer payments processed through DFAS have generally taken longer to receive than payments from other federal and private sector customers. FPI believes that ultimately, a majority of its past-due accounts receivable are fully collectable. The amount due FPI, net of allowances, from DOD for the fiscal years ended September 30, 2013 and 2012 was $23,238 and $14,525, respectively.

While federal accounts receivable are normally fully collectible in accordance with federal law, FPI has established an allowance for future losses against its federal accounts receivable to account for potential billing errors related to pricing and customer discounts, as well as instances of expired or cancelled funding from its federally appropriated customers. At September 30, 2013 and 2012, FPI's allowance for doubtful accounts is stated at approximately $412 and $519, respectively, of which approximately $206 and $98, respectively, represents the amounts allocated against federal accounts receivable.

Inventories

FPI maintains its inventory primarily for the manufacture of goods for sale to its customers. FPI's inventory is composed of three categories: Raw Materials, Work-in-Process, and Finished Goods. These categories are generally defined by FPI as follows: Raw Materials consist of materials that have been acquired and are available for the production cycle, Work-in-Process is composed of materials that have moved into the production process and have some measurable amount of labor and overhead added by FPI, Finished Goods are materials with FPI added labor and overhead that have completed the production cycle and are awaiting sale to customers.

Raw material inventory value is based upon moving average cost. Inventories are valued at the lower of average cost or market value (LCM) and include materials, labor and manufacturing overhead. Market value is calculated on the basis of the contractual or anticipated selling price, less allowance for administrative expenses. FPI values its finished goods and sub-assembly items at a standard cost that is periodically adjusted to approximate actual cost. FPI has established inventory allowances to account for LCM adjustments and obsolete items that may not be utilized in future periods.

Advances to Vendors

FPI generally does not offer advances to the public; however, where warranted, FPI will on occasion make an advance to a vendor. Historically, these advances have been insignificant and made primarily to the Industries for the Blind. Prior to issuing advances to a vendor, the Centralized Accounts Receivable section performs a review as though they were a public customer, to include performing a due diligence review to assess risk and a review of applicant financial statements. A letter of credit is obtained as needed based on the results of this review. The FPI Controller approves advances prior to their disbursement. Advances are reduced by offset to the vendor invoice as goods are delivered.

Revenue Recognition

FPI sells a wide range of products and services to a diversified base of customers, primarily governmental departments, agencies and bureaus. Revenue is generally recognized when delivery has occurred or services have been rendered, persuasive evidence of an arrangement exists, there is a fixed or determinable price, and collectability is reasonably assured. Revenue from contracts that require customer acceptance are not recognized until either customer acceptance is obtained, or upon completion of the contract. Sales returns are primarily replaced with like items and are recorded as they occur.

Revenue is recognized on multiple element agreements as a single unit of accounting for manufactured items when the product has been accepted by the customer. Revenue for services provided on behalf of FPI through an outside company is recognized when the service provider presents a valid invoice including a customer acceptance or completion notice.

FPI records as other revenue the shipping and handling costs that have been billed to customers, installation costs for FPI products, and items procured for its customers as part of procurement services provided by the Marketing, Activation, Research, and Corporate Support Branch. The cost of providing this service is recorded as a cost of other revenue.

Deferred revenue is comprised of customer cash advances, which have been paid to FPI prior to the manufacturing of goods, delivery of goods, or performance of services.

Other income includes imputed financing for retirement, health benefits and life insurance (Note 8).

Property, Plant and Equipment

Property, plant and equipment are stated at cost, net of accumulated depreciation. Depreciation is computed using the straight-line method over the following estimated useful lives:

	Years
Machinery & Equipment	2 - 25
Computer Hardware	2 - 10
Computer Software	2 - 5
Building & Improvements	24 - 40

Upon retirement or disposition of property and equipment, the related gain or loss is reflected in the statements of operations. Repairs and maintenance costs are expensed as incurred.

Taxes

As a wholly-owned corporation of the federal government, FPI is exempt from federal and state income taxes, gross receipts tax, and property taxes.

Reclassifications

Certain fiscal year 2012 financial statement line items have been reclassified to conform with the current year presentation. The reclassifications had no material effect on total assets, liabilities, equity, cumulative results of operations, or cash flows as previously reported.

(Dollars in Thousands)

Note 3. Accounts Receivable, Net

Accounts receivable, net consists of the following:

As of September 30,	2013	2012
Intragovernmental billed receivables	$ 35,468	$ 21,676
Private sector billed receivables	4,018	4,984
	39,486	26,660
Less allowance for doubtful accounts	412	519
Accounts receivable, net	$ 39,074	$ 26,141

FPI incurred bad debt expense of $(37) and $564, respectively, for the fiscal years ended September 30, 2013 and 2012.

Note 4. Inventories, Net

Inventories, net consist of the following:

As of September 30,	2013	2012
Raw materials	$ 47,462	$ 37,956
Raw materials – vehicles	4,759	27,871
Work-in-process	19,830	21,740
Finished sub-assemblies	5,681	5,503
Finished goods	27,209	42,955
Finished goods – acceptance contracts	17,084	19,645
	122,025	155,670
Less inventory allowance	26,614	26,416
Inventories, net	$ 95,411	$ 129,254

$4,759 of FPI's fiscal year 2013 and $27,871 of FPI's fiscal year 2012 raw materials balance represents vehicles and component parts for use in the fleet management retrofit product line. A majority of that inventory balance has been contracted on behalf of the Customs and Border Protection and Bureau of Immigration and Customs Enforcement of the Department of Homeland Security (DHS) for retrofit services that are performed by FPI. As part of an interagency agreement, DHS provides advance funding to FPI to procure these vehicles. Revenue is recognized by FPI at the time of shipment of retrofitted vehicles to DHS.

(Dollars in Thousands)

$17,084 of FPI's fiscal year 2013 and $19,645 of its fiscal year 2012 finished goods balance represents goods shipped to customers or their agents for unrecognized revenue due to acceptance criteria within the customer contract. The balances as of September 30, 2013 and September 30, 2012 are primarily systems furniture installations and destination acceptance contracts shipped after the cutoff date for revenue recognition.

Note 5. Property, Plant and Equipment, Net

Property, plant and equipment, net consist of the following:

As of September 30,	**2013**	**2012**
Buildings and improvements	$ 172,093	$ 177,613
Machinery and equipment	99,297	100,098
Computer hardware	2,732	2,713
Computer software	7,139	6,519
	281,261	286,943
Less accumulated depreciation	200,513	199,312
Property, plant and equipment, net	$ 80,748	$ 87,631

Depreciation and amortization expense totaled $8,650 and $10,067 for the fiscal years ended September 30, 2013 and 2012, respectively. During fiscal year 2013, FPI invested $2,058 for the purchase and construction of property, plant and equipment. During fiscal years 2013 and 2012, FPI deactivated factories in an effort to reduce excess factory capacity. As a result of these deactivations, FPI incurred losses on property plant and equipment of $120 in fiscal year 2013, and $7,293 in fiscal year 2012.

(Dollars in Thousands)

Note 6. Other Accrued Expenses

Other accrued expenses consist of the following:

As of September 30,	**2013**	**2012**
Materials in transit	$ 1,753	$ 81
Relocation travel expense	966	1,268
FECA liabilities – current portion	2,135	1,981
Financial audit expense	492	573
Telecommunication expense	1,048	1,226
Utilities	804	779
Warranty expense	388	418
Other expense	1,607	1,148
Other accrued expenses	$ 9,193	$ 7,474

Included in other expense as of September 30, 2013 and September 30, 2012 are accruals for Intra-Departmental agreements of $701 and $774 and accruals for vendor invoices of $311 and $180, respectively.

Note 7. Business Segments

FPI's businesses are organized, managed and internally reported as five operating segments based on products and services. These segments are Clothing and Textiles, Electronics, Office Furniture, Recycling, and Services. FPI is not dependent on any single product as a primary revenue source; however, it is currently predominately dependent on the federal government market for the sale of its products and services. FPI's net sales for the fiscal years ended September 30, 2013 and 2012 for each of its business segments is presented for comparative purposes:

(Dollars in Thousands)

Net Sales

For the years ended September 30,	**2013**	**2012**
Business Segment		
Clothing and Textiles	$ 235,691	$ 214,522
Electronics	128,120	177,462
Office Furniture	118,533	160,850
Recycling	17,900	15,564
Services	33,093	37,716
Net sales	$ 533,337	$ 606,114

FPI redefined its business segments from six categories to five in fiscal year 2013. The Fleet and Industrial Products business segment was consolidated into the Electronics, Office Furniture, and Services business segments. As a result, net sales for fiscal year 2012 for Electronics, Office Furniture, and Services have been reclassified for comparative purposes.

Regulatory Compliance

FPI's ability to add or to expand production of a specified mandatory product is regulated by the Federal Prison Industries Reform Act ("the Act"). The Act provides specific guidelines to FPI regarding its methodology for evaluating and reporting new or expanded products. FPI also has procedures for competitive and non-mandatory items it produces. Finally, publication of annual decisions of the FPI Board of Directors and semi-annual sales disclosures are mandated under the Act.

Note 8. Intra-Department of Justice (DOJ) / Intragovernmental Financial Activities

FPI's financial activities interact with and are dependent upon those of DOJ and the federal government as a whole. The following is a discussion of certain intra-DOJ and intragovernmental activities and their relationship with FPI:

Relationship with the Federal Bureau of Prisons

FPI and the Federal Bureau of Prisons (BOP) have a unique relationship in that the nature of their combined missions requires the sharing of facilities and responsibilities relative to the custody, training and employment of federal inmates. The Director of the BOP, who has jurisdiction over all federal penal correctional institutions, is the Chief Executive Officer (CEO). General management of FPI is provided by the Chief Operating Officer who also serves as an Assistant Director of the BOP.

The BOP provides land to FPI for the construction of its manufacturing facilities and both FPI and BOP share certain facilities, generally at no cost to FPI. In accordance with Managerial Cost Accounting Concepts a reasonable estimate of these costs as provided by the BOP is included in general expense and other income of FPI for the fiscal years ended September 30, 2013 and 2012, respectively.

Self Insurance

In accordance with federal government policy, FPI is uninsured with respect to property damage, product liability, and other customary business loss exposures. Losses incurred are absorbed as a current operating expense of FPI or, if they are induced by factors related to FPI's relationship with the Federal Prison System, may be reimbursed by BOP. Certain other costs, principally relating to personal injury claims, are paid directly by the federal government.

Federal Employees Compensation Act

The Federal Employees Compensation Act (FECA) provides income and medical cost protection to cover federal civilian employees injured on the job, employees who have incurred a work-related occupational disease, and beneficiaries of employees whose death is attributable to a job related injury or occupational disease. The United States Department of Labor (DOL), which administers FECA, annually charges each federal agency and department for its applicable portion of claims and benefits paid in the preceding year. As of September 30, 2013 and September 30, 2012, the accrued FECA liabilities as charged to FPI, approximated $2,135 and $1,981, respectively.

DOL also calculates the liability of the federal government for future claims and benefits, which includes the estimated liability of death, disability, medical, and other approved costs. Future claims and benefits are determined from an actuarial extrapolation, utilizing historical benefit payment patterns and calculations of projected future benefit payments discounted to current value over a 23.5 year period. FPI's estimated future liability approximated $21,715 and $18,920 at September 30, 2013 and 2012, respectively.

Retirement

Substantially all of FPI's civilian employees are covered under either the Civil Service Retirement System (CSRS), the Federal Employee Retirement System (FERS) or the Federal Employee Retirement System-Revised Annuity Employees (FERS-RAE) System. For employees covered by the CSRS, (those employees hired prior to January 1, 1984), for fiscal years ended September 30, 2013 and September 30, 2012, FPI contributed approximately 7 percent (for normal retirement) or 7.5 percent (for hazardous duty retirement) of each employee's salary, respectively. CSRS covered employees do not have Federal Insurance Contribution Act (FICA) withholdings and, thus, are not fully eligible to receive Social Security benefits. For employees covered by the FERS, (generally those employees hired on or after January 1, 1984), FPI contributed (for normal retirement) 11.9 percent and 11.7 percent for fiscal years ended September 30, 2013 and September 30, 2012. FPI contributed (for hazardous retirement) 26.3 percent and 25.7 percent for fiscal years ended

September 30, 2013 and September 30, 2012. For employees covered by the FERS-RAE, (generally those employees hired on or after January 1, 2013), FPI contributed (for normal retirement) 9.6 percent and 24.0 percent (for hazardous duty retirement) for the fiscal year ended September 30, 2013.

Under FERS and FERS-RAE, employees also receive retirement benefits from Social Security and, if applicable, benefits from a defined contribution plan (thrift). Under the thrift plan, an employee may contribute (tax deferred) to an investment fund, up to $17,500 of salary for the fiscal year ended September 30, 2013 and $17,000 of salary for the fiscal year ended September 30, 2012. FPI then matches this amount up to 4 percent in addition to an automatic 1 percent that is contributed for all FERS and FERS-RAE employees. Those employees that elected to remain under CSRS after January 1, 1984 continue to receive benefits in place, and may also contribute (tax deferred) up to $17,500 of their salary to the thrift plan for the fiscal year ended September 30, 2013 and up to $17,000 of salary for the fiscal year ended September 30, 2012, but with no automatic or matching amount contributed by FPI.

CSRS, FERS, and FERS-RAE are multi-employer plans. Although FPI funds a portion of pension benefits relating to its employees, and provides for the necessary payroll withholdings, it does not maintain or report information with respect to the assets of the plans, nor does it report actuarial data with respect to accumulated plan benefits or the pension liability relative to its employees. The reporting of such amounts is the responsibility of the United States Office of Personnel Management (OPM).

FPI's contribution to both plans was approximately $25,253 and $26,855 for the fiscal years ended September 30, 2013 and September 30, 2012, respectively.

FPI must recognize its share of the cost of providing pension benefits to eligible employees utilizing cost factors determined by the OPM. Included in general and administrative expense is approximately $2,362 and $2,423 in the fiscal years ended September 30, 2013 and 2012, respectively, with an offsetting credit to other income on the Statements of Operations and Cumulative Results of Operations.

Health Benefits and Life Insurance

FPI, through the OPM, offers health and life insurance plans under which premium costs for health care are shared between FPI and the employees. A substantial portion of life insurance premiums are paid for by employees. Amounts paid by FPI for health benefits and life insurance approximated $9,407 and $9,717 for the fiscal years ended September 30, 2013 and 2012, respectively.

OPM also provides health care and life insurance benefits for FPI's retired employees. FPI must recognize an expense related to its share of the cost of such post-retirement health benefits and life insurance on a current basis (while its employees are still working), with an offsetting credit to other income. Costs in this regard, which approximated $5,127 and $6,420 during the fiscal years ended September 30, 2013 and 2012, respectively, were determined by OPM utilizing cost factors to estimate the cost of providing post-retirement benefits to current employees. However, because of the offsetting credit, which is reflected as other income on the Statements of Operations and Cumulative Results of Operations, the recording of these costs has no impact on reported net income or cash flows.

(Dollars in Thousands)

Future post-retirement health care and life insurance benefit costs are not reflected as a liability on FPI's financial statements, as such costs are expected to be funded in future periods by OPM.

Note 9. Sales and Marketing, General and Administrative Expenses

Sales and marketing, general and administrative expenses consist of the following:

Fiscal years ended September 30,	**2013**	**2012**
Salaries, wages and benefits	$ 39,494	$ 42,986
Permanent change of station expense	743	1,657
Purchases of minor equipment	495	172
Contract services	7,625	9,270
Bad debt expense	(37)	564
Credit card service fees	716	970
Travel	1,063	1,487
Personal computer expense	1,315	1,458
Accident compensation	4,881	4,660
Financial audit	1,131	1,257
Marketing	1,261	1,550
Depreciation	1,496	2,122
Loss on disposition of assets	291	7,549
Gain on disposition of assets	(29)	(33)
Telecommunication expense	2,451	2,914
Other expense	(4,987)	(4,290)
Imputed pension costs (Note 8)	2,362	2,423
Imputed post-retirement health care and life insurance cost (Note 8)	5,127	6,420
Imputed operating costs	21,069	24,718
Sales and marketing, general and administrative expenses	$ 86,467	$ 107,854

Other expense is comprised primarily of inmate wages, maintenance agreements, and distributions to factory operations. FPI distributes certain General and Administrative expenses that benefit all locations to the individual factory levels. These charges include computer licenses and fees, civilian and inmate accident compensation, and check charges. These charges totaled $7.4 million for fiscal year 2013 and $7.7 million for fiscal year 2012. Contract services consist primarily of consulting and sales and marketing fees. Salaries, wages and benefits are shown net of the imputed financing offsetting credit (Note 8). Included in accident compensation for fiscal year 2013 is a $2.8 million increase in the actuarial FECA estimated liability.

(Dollars in Thousands)

Note 10. Commitments and Contingencies

Legal Contingencies

FPI is party to various administrative proceedings, legal actions, and claims. The balance sheet includes an estimated liability for those legal actions where management and the FPI General Counsel consider adverse decisions "probable" and amounts are reasonably estimable. Legal actions where management and the FPI General Counsel consider adverse decisions reasonably possible and the amounts are reasonably estimable, should not result in judgments which would have a material, adverse effect on the organization's financial statements. Furthermore, there are cases where amounts have not been accrued or disclosed because the amounts of the potential loss cannot be estimated or the likelihood of an unfavorable outcome is considered remote.

Lease Commitments

FPI leases certain facilities, machinery, vehicles and office equipment under noncancelable capital and operating lease agreements that expire over future periods. Many of these lease agreements provide FPI with the option (after initial lease term) to either purchase the leased item at the then fair value or to renew the lease for additional periods of time. As of September 30, 2013, future capital lease payments due and future operating lease commitments total $75 and $209, respectively.

Product Warranty

FPI offers its customers a promise of an "Escape Proof Guarantee" on the products it manufactures. FPI has analyzed the historical pattern of warranty returns and the adequacy of the warranty returns and allowances. In this regard, FPI has established an estimate of future warranty returns related to current period product revenue.

Changes in aggregate product warranty liability

Fiscal years ended September 30,	**2013**	**2012**
Balance at the beginning of the period	$ 418	$ 444
Accruals for warranties issued during the period	253	349
Settlements made (in cash or in kind) during the period	(283)	(375)
Balance at the end of the period	$ 388	$ 418

Congressional Limitation on Administrative Expenses

Congress has imposed an annual spending limit on certain administrative expenses relating to FPI's central office management. These costs include salaries for management personnel, travel expenses and supplies. The following is a comparison of actual expenses to the limitation imposed:

Fiscal years ended September 30,	**2013**	**2012**
Congressional limitation on expenses	$ 2,700	$ 2,700
Expenses incurred subject to Congressional limitation	$ 2,170	$ 1,760