FEDERAL PRISON INDUSTRIES, INC.

Fiscal Year 2020

Annual Management Report

November 13, 2020

U.S. Department of Justice

UNICOR

Federal Prison Industries, Inc.

Washington, DC 20534

November 13, 2020

We are pleased to present the Federal Prison Industries, Inc.'s (FPI) Fiscal Year 2020 Annual Management Report to the Congress of the United States. This report includes FPI's financial statements, Management's Discussion and Analysis, the Office of the Inspector General Commentary and Summary, and the Independent Auditors' report on the Corporation's financial statements, including internal controls over financial reporting and compliance, and other matters. FPI's financial statements received an unmodified opinion, although a material weakness related to revenue presentation was identified. FPI will assemble an ASC 606 team to assess, change, and implement policies and procedures necessary to ensure compliance with ASC 606 Revenue from Contracts with Customers.

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 these years remains the same - to protect society and reduce crime by preparing inmates for successful reentry through job training. FPI continues to emphasize reaching as many inmates as possible by focusing on the employment of inmates within three years of release. As one of the Bureau of Prisons'(BOP's) most crucial inmate reentry programs, FPI employed almost 16,500 inmates throughout FY 2020, employing 9,452 federal inmates 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. They 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 US economy through the raw materials purchased from suppliers, including veteran, small, and women-owned businesses; 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. It 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, the emphasis continues to be exploring more opportunities with commercial customers. New market authorities, contained in both the Consolidated and Further Continuing Appropriations Act of 2012 (PL 112-55) and PL 112-55 authorizing FPI to participate in the Prison Industries Enhancement Certification Program (PIECP) are now available for FPI to obtain commercial customers through repatriation and bringing work opportunities otherwise performed outside of the United States. Additionally, FPI is in the process of implementing the new authorities provided by the First Step Act in the fiscal year 2019. FPI is optimistic that we will continue to grow operations as we seek to meet the employment goals outlined in the First Step Act. 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. The outstanding dedication of FPI staff, the continued outstanding support, and leadership provided by the Board of Directors all contribute to FPI's continued success.

Michael D. Carvajal

Director
Federal Bureau of Prisons
Commissioner of FPI

Patrick T. O'Connor

Chief Executive Officer
Federal Prison Industries, Inc.

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 Commissioner of FPI. General management of FPI is provided by the Chief Executive Officer who also serves as an Assistant Director for the BOP.

In fiscal year 2020, FPI operated in seven business segments: Agribusiness, Clothing and Textiles, Electronics, Fleet, Office Furniture, Recycling, and Services. FPI has agricultural, industrial and service operations at 63 factories and 2 farms located at 52 prison facilities as of September 30, 2020. 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 primarily from the private sector to produce finished goods. Orders for goods and services are obtained through marketing and sales efforts managed primarily 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 in 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 and staff salaries 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 for fiscal year 2020 include the Department of Defense (DOD), the Department of Justice (DOJ), the Department of Homeland Security (DHS), the Social

Security Administration (SSA), and the Department of Agriculture (DOA).

Due to the volatile nature of the changes affecting FPI 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 and the 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 and continues to invest significant time and effort into pursuing this goal in fiscal year 2020 through research and discussion within the organization and other agencies.

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 (GAAP) based on accounting standards issued by the Financial Accounting Standards Board (FASB), the private sector standards-setting body. GAAP requires 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 from contracts with multiple element arrangements is recognized as each element is earned based on the relative fair value of each element provided the delivered elements have value to customers on a standalone basis and amounts can be allocated to each element based on its objectively determined fair value. Otherwise, revenue is recognized on multiple element agreements as a single unit of accounting when the product has been accepted by the customer.

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 this 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.

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, and 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 net realizable value (LCNRV) and include materials, labor and manufacturing overhead. Net realizable 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 LCNRV 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 reentry 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 86 years. Over the course of these years, FPI has positively impacted countless staff and inmate lives. 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 an active role in their rehabilitation. 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 Cash Equivalents

Cash and Cash Equivalents decreased $43.6 million during fiscal year 2020. The primary factor in the decrease in cash, related to a $98.9 million dollar increase in inventory from 2019. The inventory increase was driven by a $72.2 million increase in vehicles for the Fleet Business Group. The increase in inventory was partially offset by $43.4 million investments redeemed, as well as a $33.6 million increase in deferred revenue.

Investments

During fiscal year 2020, FPI redeemed $43.4 million in investments. As a general investment strategy, FPI plans to hold all short-term and long-term investments to maturity.

Accounts Receivable

The Accounts Receivable balance decreased $3.5 million during fiscal year 2020. FPI's average days to collect in 2020 were approximately 25 days. The accounts receivable balance over sixty days old represented 41.1% of the total balance as of September 2020.

Liabilities

Total Liabilities increased by $31.8 million during fiscal year 2020. The primary contributor was a $33.6 million increase in deferred revenue. The increase in deferred revenue is primarily attributable to a change in customer advances payable on hand primarily for the retrofitting of vehicles for the Department of Homeland Security.

Revenue, Cost of Revenue, COVID-19, and Net Loss

Total revenue decreased by $171.4 million while total cost of revenue decreased $146.3 million. The COVID-19 pandemic significantly impacted sales during fiscal year 2020. Prior to the pandemic, net sales for the first 6 months of the year totaled nearly $231 million, or approximately 64% of the annual total. After the start of the pandemic, sales for the last 6 months plummeted to just $132 million or 36% of the total. COVID-19 had a similar effect in the earnings and net loss for 2020. The first 2 quarters, before the COVID-19 shutdowns, showed FPI earnings of $8.5 million, or approximately $1.4 million per month. After the effects of COVID-19, FPI lost $11.5 million over the final 6 months of 2020, or a loss of approximately $1.9 million per month.

Business Segments

In fiscal year 2020, FPI's businesses were organized, managed, and internally reported as seven operating segments based on products and services. These segments are Agribusiness, Clothing and Textiles, Electronics, Fleet, 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 sales for fiscal year 2020, were greatly impacted by the COVID-19 pandemic. Prior to the pandemic, net sales for the first 6 months of the year totaled nearly $231 million, or approximately 64% of the annual total. After the pandemic, sales for the last 6 months plummeted to just $132 million or 36% of the total. FPI's net industrial income (earnings) at the business segment level consists of sales offset by cost of goods sold and certain other general and administrative costs.

The amounts listed in the table below are presented as dollars in thousands.

Business Segment	Fiscal Year	
Agribusiness	**2020**	**2019**
Net Sales	$7,673	$6,436
Earnings	$136	$(1,064)
Clothing and Textiles		
Net Sales	$121,923	$127,242
Earnings	$1,878	$11,265
Electronics		
Net Sales	$21,321	$37,885
Earnings	$4,452	$9,423
Fleet		
Net Sales	$85,262	$138,992
Earnings	$5,592	$9,747
Office Furniture		
Net Sales	$81,381	$99,540
Earnings	$7,869	$11,353
Recycling		
Net Sales	$17,473	$17,064
Earnings	$9,153	$8,439
Services		
Net Sales	$28,191	$39,588
Earnings	$5,047	$12,003
Factory Total		
Net Sales	$363,224	$466,747
Earnings	$34,127	$61,166

Possible Future Effects of Existing Events and Conditions

During fiscal year 2020, COVID-19 had a negative impact on the anticipated growth from the preceding four years. FPI realized a loss of $3 million at the end of fiscal year 2020. The total cash and investment balance decreased $87.3 million during fiscal year 2020, to a total balance of $298.9 million. Net inventory increased from $109.3 million to $208.1 million. Fiscal year 2020 net sales were significantly below plan (-36.3%). During the first half of the year, with sales of $230.8 million, FPI was only 7.3% below sales plan. However, after the COVID-19 pandemic began, sales for the last half of the year fell to only $132.4 million, which was 58.8% below plan for that period.

ASC Topic 606 – Revenue from Contracts with Customers

In May 2020, the Financial Accounting Standards Board (FASB) voted to extend by one year the effective date of its revenue recognition standard to all nonpublic entities that have not yet issued their financial statements. The final Accounting Standards Update (ASU) allows nonpublic entities the option of adopting the revenue recognition standard (FASB ASC Topic 606, Revenue from Contracts with Customers) on the current implementation date or deferring implementation for one year.

FPI has opted to delay the adoption of ASC 606 until fiscal year 2021.

Continuing Impact of COVID-19 on FPI Operations

In fiscal year 2021, FPI will continue to work on recovering from the unprecedented disruptions to its operations due to the COVID-19 pandemic. The disruptions began at the end of March 2020, when all FPI factories were closed, except those converted to the production of personal protective equipment (PPE) and two farm operations. Between April and July 2020 there were limited reopenings, but factory capacity operated at an average of only 30%, well below breakeven. By the end of September 2020, FPI was still operating at only 60% of pre-pandemic levels due to necessary COVID-19 operational restrictions.

These restrictions had a negative impact on FPI's ability to manufacture and ship products to customers in a timely manner. Additionally, many customers were unable to accept deliveries, as they were either working a modified schedule or non-operational, due to the pandemic.

The recovery, defined as reaching pre-pandemic operational levels, is anticipated to take 6 months to 1 year, though this estimate is dependent on improving pandemic conditions. Driving this recovery will continue to be the exceptional efforts of FPI staff and inmate workers under extraordinary circumstances.

FPI will continue to see sales growth as we satisfy customer demands and continue to seek opportunities to expand existing and new product lines. During fiscal year 2020, FPI secured several new contracts or modifications to current contracts that are expected to generate more than $96 million in sales over the next five years. FPI continues to pursue new business leads to assist with our strategic plan of corporate growth potential of 10% per year, over the next five years.

Plan for Growth

In order to increase sales in fiscal year 2021 and beyond, FPI's strategy is to increasingly leverage its Business Development Group (BDG). The BDG is the branch within FPI that explores and acquires commercial opportunities for FPI that are authorized under various authorities (including the First Step Act, repatriation, and the Prison Industry Enhancement Certification Program (PIECP)), in addition to identifying and securing prime and subcontracting roles on federal government contracts. In the next five years, FPI plans to leverage the BDG to increase revenues by 8% to 10% annually, which is expected to result in the activation of six FPI factories and hundreds of new inmate jobs every year once FPI has recovered from the impact of the COVID-19 pandemic.

FPI is also utilizing the expertise of several third-party resources across business operations. This includes contracting with an information technology service provider to develop a digital marketing strategy; a lead generator organization to identify businesses that can manufacture products at FPI factories under FPI’s repatriation and PIECP authorities; a procurement advisory firm to assist in securing federal government contracts for FPI, primarily in FPI’s Clothing and Textiles Business Group; and a consulting group to assist FPI in increasing its sales in the federal government and commercial optic markets. Additionally, FPI is using GovWin, a procurement intelligence database, to increase sales to government agencies, and Salesforce customer relationship management software to optimize customer relationships.

Upgrade to SAP S/4 Enterprise Resource Planning (ERP) System

In fiscal year 2019, FPI began the implementation of SAP S/4 Hana, an upgrade to FPI’s current enterprise resource planning (ERP) system. The goals of the upgrade are to implement a modern system, since the current ECC 6.0 system is nearing the end of product support, and enhance functionality in the areas of a unified general ledger, costing, and profitability analysis. The upgraded system will provide FPI users with a much more user-friendly and powerful tool, which will provide real-time data and additional analytics and allow FPI management to easily measure performance factors and implement changes to operations.

SAP S/4 Hana will improve the intuitive workflows within a cloud-based platform. Pursuing a cloud-based infrastructure is a major government-wide initiative as well as a cost-saving measure. It is estimated that operating in a cloud-based environment will save operating costs for bandwidth at FPI’s four Regional Data Centers, reduce staff costs to maintain hardware, and reduce data charges at our Department of Justice Data Centers. Savings estimates range from $0.5 to $1 million.

The upgrade to SAP S/4 Hana is a corporate-wide initiative, which requires support from all business segments, as well as significant database cleanup, and an extensive coordination of efforts and will be implemented at the beginning of fiscal year 2022.

Inmate Employment

FPI employed 16,478 inmate workers throughout fiscal year 2020, which, due to COVID-19, was below FPI’s goal of 18,000 inmate workers. FPI's goal is that 30% of the FPI inmate workforce consists of inmates within 3 years of their release date. Exposing inmates to the FPI experience, helps enhance inmate's post-release job prospects by building FPI work skills prior to release. For fiscal year 2020, 32% of FPI inmates were within 3 years of their release, exceeding the target rate.

By fiscal year 2022, the First Step Act requires the Attorney General to report on efforts to enable 75% of the eligible minimum- and low-risk offenders to have the opportunity to participate in a prison work program for not less than 20 hours per week. FPI will be expected to grow in order to provide a significant number of these opportunities.

COMMENTARY AND SUMMARY

Audit of the Federal Prison Industries, Inc. Annual Financial Statements Fiscal Year 2020

Objectives

Pursuant to the Government Corporation Control Act, as amended (31 U.S.C. § 9105), the Department of Justice Office of the Inspector General (OIG) is required to perform or contract an independent auditor to perform an audit of the Federal Prison Industries, Inc.'s (FPI) annual financial statements.

The objectives of the audit are to opine on the financial statements; report on internal control over financial reporting; and report on compliance and other matters, including compliance with the Federal Financial Management Improvement Act of 1996 (FFMIA).

Results in Brief

KPMG LLP (KPMG) found that the FPI's financial statements are fairly presented as of and for the year ended September 30, 2020. An unmodified opinion was issued. KPMG identified one material weakness in the Independent Auditors' Report. The Independent Auditors' Report did not report any instances of non-compliance.

The OIG reviewed KPMG's report 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 FFMIA, or conclusions on compliance and other matters. KPMG is responsible for the attached Independent Auditors' Report dated November 13, 2020, and the conclusions expressed in the report. Our review disclosed no instances where KPMG did not comply, in all material respects, with auditing standards generally accepted in the United States of America.

Recommendations

KPMG provided FPI one recommendation to improve FPI's internal control over revenue recognition.

Audit Results

Under the direction of the OIG, KPMG performed the FPI's audit in accordance with auditing standards generally accepted in the United States of America. The fiscal year (FY) 2020 audit resulted in an unmodified opinion on the financial statements. An unmodified opinion means that the financial statements present fairly, in all material respects, the financial position and the results of the entity's operations in accordance with U.S. generally accepted accounting principles. For FY 2019, the FPI also received an unmodified opinion on its financial statements (OIG Audit Division Report No. 20-018).

KPMG reported a material weakness in the FY 2020 Independent Auditors' Report, noting that improvements are needed in the revenue presentation controls.

No instances of non-compliance or other matters were identified during the audit that are required to be reported under Government Auditing Standards. Additionally, KPMG's tests disclosed no instances in which the FPI's financial management systems did not substantially comply with FFMIA.

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

Independent Auditors' Report

Inspector General
U.S. Department of Justice

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

Report on the Financial Statements

We have audited the accompanying financial statements of the U.S. Department of Justice Federal Prison Industries, Inc. (FPI), which comprise the balance sheets as of September 30, 2020 and 2019, and the related statements of operations and cumulative results of operations, and cash flows for the years 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 audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America, in accordance with the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, and in accordance with Office of Management and Budget (OMB) Bulletin No. 19-03, *Audit Requirements for Federal Financial Statements*. Those standards and OMB Bulletin No. 19-03 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 auditor considers 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

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, 2020 and 2019, and the results of its operations and its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

Other Matters

Other Information

Our audits were conducted for the purpose of forming an opinion on the basic financial statements as a whole. The Management's Discussion and Analysis section 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 audits 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

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements as of and for the year ended September 30, 2020, we considered FPI's internal control over financial reporting (internal control) as a basis for designing 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 FPI's internal control. Accordingly, we do not express an opinion on the effectiveness of 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*.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. However, as described in the Exhibit, we did identify a deficiency in internal control that we consider to be a material weakness.

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. We consider the deficiency described in the Exhibit to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether FPI's financial statements as of and for the year ended September 30, 2020 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 financial statements. 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 disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* or OMB Bulletin No. 19-03.

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 disclosed no instances in which FPI's financial management systems did not substantially comply with the (1)

Federal financial management systems requirements, (2) applicable Federal accounting standards, and (3) the United States Government Standard General Ledger at the transaction level.

FPI's Response to Findings

FPI's response to the findings identified in our audits are described in the Exhibit. FPI's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the response.

Purpose of the Other Reporting Required by Government Auditing Standards

The purpose of the communication described in the Other Reporting Required by *Government Auditing Standards* section is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of FPI's internal control or compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

Washington, D.C.
November 13, 2020

Material Weakness

This section contains our discussion of the material weakness that we identified in internal control over financial reporting.

Improvements Needed in Revenue Presentation Controls

Federal Prison Industries, Inc. (FPI) provides employment and training for inmates in the Federal Prison System while remaining self-sufficient through the sale of its products and services primarily to governmental departments, agencies, and bureaus. When FPI manufacturers and sells its own products, the revenue is shown in the net sales line and the cost of the revenue is shown as the cost of sales. Presenting these two amounts separately is referred to as gross presentation. FPI, in certain cases, also provides procurement services through its Services Interagency Contracting Group (SICG). When FPI facilitates a transaction for others as an agent but is not the principal of the transaction, the revenue and cost should be presented as a single net amount, referred to as net presentation.

FPI's internal controls over revenue presentation for principal/agent transactions were deficient. Management did not accurately classify revenue from contracts that should be recorded on a net basis as an agent of the transaction. FPI did not identify the need to reassess its revenue presentation policy despite a material increase in activity in its SICG. At the end of FY 2020, FPI incorrectly presented $79 million of revenue transactions on a gross basis that should have been presented on a net basis. Management subsequently corrected the error in the year-end financial statements. Net position was unchanged by the correction.

Criteria:

The Government Accountability Office's *Standards for Internal Controls in the Federal Government* states:

> Principle 9.01 (Identify, Analyze, and Respond to Change): "Management should identify, analyze, and respond to significant changes that could impact the internal control system."

The Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) states:

> Section 605-45-05-1 (Overview and Background): "This Subtopic provides guidance as to whether an entity should report revenue gross or net of certain amounts paid to others. The reporting depends on whether the entity functions as principal or agent."

In the fiscal year 2021, FPI is required to implement FASB ASC Section 606 for revenue recognition.

Recommendation*:*

We recommend that FPI implement policies and procedures to assess significant changes in their operations and enhance their training programs to enable their staff to identify and respond to required accounting principles, including FASB ASC Section 606, in the fiscal year 2021.

Management Response:

Management concurs with this recommendation. FPI will assemble an ASC 606 team to assess, change, and implement policies and procedures necessary to ensure compliance with the ASC 606 Revenue Recognition standards. This interdisciplinary team will consist of Financial Management, Procurement, Business Group/Branch, Legal Counsel, and the RSM consulting firm. Additional manpower and technical resources shall be made available to the ASC 606 team as they identify needs.

Federal Prison Industries, Inc.

Balance Sheets

As of September 30, *(DOLLARS IN THOUSANDS)*	2020	2019
Assets		
Current:		
Cash and cash equivalents	$ 174,605	$ 218,209
Accounts receivable, net	36,109	39,598
Short term investments	58,873	43,872
Inventories, net	208,132	109,276
Other assets	9,608	5,261
Total current assets	487,327	416,216
Investments	65,450	124,124
Property, plant and equipment, net	71,281	54,872
Total long term assets	136,731	178,996
Total Assets	$ 624,058	$ 595,212
Liabilities and United States Government Equity		
Current:		
Accounts payable	$ 34,404	$ 37,915
Deferred revenue	182,949	149,398
Accrued salaries and wages	5,962	6,023
Accrued annual leave	5,585	5,038
Other accrued expenses	12,608	9,752
Total current liabilities	241,508	208,126
FECA actuarial liability	20,955	22,496
Total Liabilities	262,463	230,622
United States Government Equity		
Initial capital	4,176	4,176
Contributed capital	6,905	6,905
Cumulative results of operations	350,514	353,509
Total United States Government Equity	361,595	364,590
Total Liabilities and United States Government Equity	$ 624,058	$ 595,212

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)***	**2020**	**2019**
Revenue:		
Net sales	$ 363,224	$ 466,747
Other revenue	110,177	178,087
Total revenue	473,401	644,834
Cost of revenue:		
Cost of sales	335,324	411,679
Cost of other revenue	102,402	172,302
Total cost of revenue	437,726	583,981
Gross profit	35,675	60,853
Operating expenses:		
Sales and marketing	2,945	3,741
General and administrative	68,713	75,386
Total operating expenses	71,658	79,127
Loss from operations	(35,983)	(18,274)
Interest income	4,052	6,098
Interest expense	(5)	(8)
Other income, net	28,941	33,014
Net income/ (loss)	(2,995)	20,830
Cumulative results of operations, beginning of fiscal year	353,509	332,679
Cumulative results of operations, end of fiscal year	$ 350,514	$ 353,509

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)***	**2020**	**2019**
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Income	$ (2,995)	$ 20,830
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	5,547	5,847
Amortization of discount or premium on investments	254	(773)
Loss on disposal of property, plant and equipment	658	1,538
Changes in:		
Accounts receivable	3,489	(5,461)
Inventories	(98,856)	12,395
Other assets	(4,347)	2,870
Accounts payable and accrued expenses	(1,710)	1,513
Deferred revenue	33,551	38,484
Net cash provided by (used in) operating activities	(64,409)	77,243
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property, plant and equipment	(22,614)	(11,190)
Investments redeemed	43,419	48,660
Net cash provided by investing activities	20,805	37,470
Net increase (decrease) in cash and cash equivalents	(43,604)	114,713
Cash and cash equivalents, beginning of fiscal year	218,209	103,496
Cash and cash equivalents, end of fiscal year	$ 174,605	$ 218,209

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

Fiscal Years 2020 and 2019
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 (fiscal year 2020 percent of Revenue shown in parenthesis), agencies and bureaus such as the Department of Defense (55%), the Department of Justice (19%), the Department of Homeland Security (16%), the Social Security Administration (5%), and the Department of Agriculture (1%). 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 agricultural, industrial, and service operations at 63 factories and 2 farms located at 52 prison facilities that employed 9,452 and 10,998 inmates as of September 30, 2020 and 2019, 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 (GAAP) 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 U.S. GAAP. FASAB allows certain government agencies that have historically used FASB standards to continue to utilize FASB standards for Financial Statement presentations.

Use of Estimates

The preparation of financial statements in conformity with U.S. 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 with an original maturity of three months or less to be cash equivalents. In fiscal year 2020, FPI's investment activities and cash equivalents included overnight repurchase agreements with the Bureau of the Fiscal Service of the United States Treasury. The market value of overnight purchase agreements is equivalent to cost.

Fair Value Measurements

FASB Accounting Standard Codification (ASC) 820-10, Fair Value Measurements and Disclosures, establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The FPI's financial instruments are comprised of cash, accounts receivable, accounts payable, and accrued liabilities as of September 30, 2020 and 2019, respectively. The carrying amounts of these financial instruments approximate fair value because of the short-term nature of these instruments. The FPI intends to hold their investments until maturity, and therefore, has recorded the investments at amortized cost.

Investments

FPI invests in Treasury fixed-principal notes with Bureau of the Fiscal Service of the United States Treasury. Treasury fixed-principal notes are issued with a stated rate of interest to be applied to their par amount, have interest payable semiannually, and are redeemed at their par amount at maturity. All investments with maturity due dates within the next fiscal year are considered short-term, and classified as current assets. FPI plans to hold these investments to maturity.

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. At September 30, 2020 and 2019, FPI's allowance for doubtful accounts is stated at approximately $610 and $701.

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. Most of the 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 taken longer to receive than payments from other federal and private sector customers. The amount due to FPI from DOD for the fiscal years ended September 30, 2020 and 2019 was $24,553 and $28,088, respectively.

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, and 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 is valued at moving average cost. Inventories are valued at the lower of cost or net realizable value (LCNRV) and include materials, labor and manufacturing overhead. Net realizable 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 LCNRV adjustments and excess, obsolete, or unserviceable inventory 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. Prior to issuing advances to a vendor, the Centralized Accounts Receivable office performs a review as though the vendor is 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 from contracts with multiple element arrangements is recognized as each element is earned based on the relative fair value of each element provided the delivered elements have value to customers on a standalone basis and amounts can be allocated to each element based on its objectively determined fair value. Otherwise, revenue is recognized on multiple element agreements as a single unit of accounting when the product has been accepted by the customer.

FPI records as other revenue the shipping and handling costs that have been billed to customers, installation costs for FPI furniture products, service contracts in the Fleet Business Group, and items procured for its customers as part of procurement services provided by the Services Interagency Contracting Group. 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, life insurance, and BOP operating expenses (Note 9).

Property, Plant and Equipment

Property, plant and equipment are stated at cost, net of accumulated depreciation. Under FPI's current policy, 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
Livestock	4
Building & Improvements	24 - 40

There are several assets that have lives longer than those stated above; however, they were established prior to the current policy.

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.

FPI values livestock, including new cattle born into the herd at lower of cost or net realizable value (LCNRV) until they are either sold or die. Costs for cattle under development are accumulated throughout their development cycle. For dairy cattle, the development period is 22 months, which is the average age of maturity for a productive heifer. At this point the cow is considered a capital asset and the LCNRV analysis can be conducted and the asset properly valued. All beef cattle accumulate costs on a monthly basis until sale or death has occurred. A gain or loss will be recognized on all beef cattle at the time of death or sale.

(Dollars in Thousands)

Agribusiness livestock, property, plant and equipment will be depreciated using straight-line depreciation along with the standard useful life structure noted above.

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.

Reclassification of Prior Year Presentation

Certain prior year amounts have been reclassified for consistency with the current year presentation. These reclassifications had no effect on the reported results of operations. An adjustment has been made to the presentation of Other Revenue ($64.7 million) and Cost of Other Revenue ($61.7 million) as it relates to the service contracts in Fleet Business Group. Amounts previously recorded as Sales and Cost of Sales, have been reclassified to Other Revenue and Cost of Other Revenue.

Subsequent Events

Subsequent events are evaluated by management through the date that the financial statements are available to be issued, which is November 13, 2020.

Note 3. Investments

The amortized cost and maturities of investment securities were as follows:

As of September 30,	**2020**	**2019**
Due in one year or less	$ 58,873	$ 43,872
Due after one year through five years	65,450	124,124
	$ 124,323	**$ 167,996**

The investments above held by FPI at September 30, 2020 and 2019 consist of Market Notes, issued by the U.S. Treasury. All of these notes are either explicitly or implicitly backed by the U.S. Government. Given the backing by the U.S. Government, current market conditions have not had a significant adverse impact on the fair value of these securities.

As of September 30, 2020, no investments are in an unrealized loss position.

(Dollars in Thousands)

Note 4. Accounts Receivable, Net

Accounts receivable, net consists of the following:

As of September 30,	2020	2019
Intragovernmental receivables	$ 34,294	$ 34,178
Interest receivable – investments	424	506
Private sector receivables	2,001	5,615
	36,719	40,299
Less allowance for doubtful accounts	610	701
Accounts receivable, net	$ 36,109	$ 39,598

FPI incurred bad debt expense of $53 and $159, respectively, for the fiscal years ended September 30, 2020 and 2019.

Note 5. Inventories, Net

Inventories, net consists of the following:

As of September 30,	2020	2019
Raw materials	$ 156,218	$ 67,579
Work-in-process	19,076	14,989
Finished sub-assemblies	7,878	5,601
Finished goods	27,308	21,576
Finished goods – acceptance contracts	2,892	2,840
	213,372	112,585
Less inventory allowance	5,240	3,309
Inventories, net	$ 208,132	$ 109,276

Approximately $2,892 of FPI's fiscal year 2020 and $2,840 of its fiscal year 2019 finished goods balance represents goods shipped to customers or their agents, and is unrecognized revenue due to acceptance criteria within the customer contract.

(Dollars in Thousands)

Note 6. Property, Plant and Equipment, Net

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

As of September 30,	2020	2019
Buildings and improvements	$ 173,903	$ 173,015
Machinery and equipment	85,577	95,504
Livestock	3,153	2,768
Computer hardware	2,078	2,084
Computer software	7,601	7,601
	272,312	280,972
Less accumulated depreciation	224,729	232,520
	47,583	48,452
Software under development	23,598	5,797
Construction in progress	100	623
Property, plant and equipment, net	$ 71,281	$ 54,872

Depreciation and amortization expense totaled $5,547 and $5,847 for the fiscal years ended September 30, 2020 and 2019, respectively. During fiscal years 2020 and 2019, FPI invested $22,614 and $11,190, respectively, for the purchase and construction of property, plant and equipment.

Note 7. Other Accrued Expenses

Other accrued expenses consist of the following:

As of September 30,	2020	2019
Materials in transit	$ 403	$ 556
Relocation travel expense	539	534
FECA liabilities – current portion	1,374	1,754
Financial audit expense	883	1,189
Telecommunication expense	1,867	834
Utilities	767	1,255
Product warranties	311	316
Intra-Departmental agreements	913	475
Vendor invoices	5,152	2,577
Other expense	399	262
Other accrued expenses	$ 12,608	$ 9,752

(Dollars in Thousands)

Note 8. Business Segments

FPI's businesses are organized, managed and internally reported as seven operating segments based on products and services. These segments are Agribusiness, Clothing and Textiles, Electronics, Fleet, 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 sales for fiscal year 2020, were greatly impacted by the COVID-19 pandemic. Prior to the pandemic, net sales for the first 6 months of the year totaled nearly $231 million, or approximately 64% of the annual total. After the pandemic, sales for the last 6 months plummeted to just $132 million or 36% of the total.

FPI's net sales for the fiscal years ended September 30, 2020 and 2019 for each of its business segments is presented for comparative purposes:

Net Sales

For the fiscal years ended September 30,	**2020**	**2019**
Business Segment		
Agribusiness	$ 7,673	$ 6,436
Clothing and Textiles	121,923	127,242
Electronics	21,321	37,885
Fleet	85,262	138,992
Office Furniture	81,381	99,540
Recycling	17,473	17,064
Services	28,191	39,588
Net sales	$ 363,224	$ 466,747

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 9. 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 financial activities and their relationship with FPI:

Relationship with the Federal Bureau of Prisons

FPI and the 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 Commissioner of Federal Prison Industries. General management of FPI is provided by the Chief Executive 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 an 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, 2020 and 2019, 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, 2020 and 2019, the accrued FECA liabilities as charged to FPI, approximated $1,374 and $1,754, respectively.

FPI is required by generally accepted accounting principles (GAAP) to account for future workers' compensation costs not yet paid. These costs include employees' medical expenses, payments for continuation of wages, estimated liability of death, and DOL administrative fees. The liability amount is determined by discounting the projected annual benefit payments using Treasury spot rates. FPI's estimated future liability approximated $20,955 and $22,496 as of September 30, 2020 and 2019, 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, 2020 and 2019, 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 between January 1, 1984 and December 31, 2012), FPI contributed (for normal retirement) 16.0 percent and 13.7 percent for fiscal years ended September 30, 2020 and 2019 respectively. FPI contributed (for hazardous retirement) 33.4 percent and 30.1 percent for fiscal years ended September 30, 2020 and 2019 respectively. For employees covered by the FERS-RAE, (generally those employees hired between January 1, 2013 and December 31, 2013), FPI contributed (for normal retirement) 14.2 percent and 11.9 percent for fiscal years ended September 30, 2020 and 2019 respectively. FPI contributed (for hazardous duty retirement) 31.6 percent and 28.4 percent for the fiscal years ended September 30, 2020 and 2019 respectively. For employees covered by the FERS-FRAE, (generally those employees hired on or after January 1, 2014), FPI contributed (for normal retirement) 14.2 percent and 11.9 percent for fiscal years ended September 30, 2020 and 2019 respectively. FPI contributed (for hazardous duty retirement) 31.6 percent and 28.4 percent for the fiscal years ended September 30, 2020 and 2019 respectively.

Under FERS, FERS-RAE, and FERS-FRAE employees also receive retirement benefits from Social Security and, if applicable, benefits from a defined contribution plan (thrift savings plan). Under the thrift plan, an employee may contribute (tax deferred) to an investment fund, up to $19,500 and $19,000 of salary for the fiscal years ended September 30, 2020 and 2019, respectively. FPI then matches this amount up to 4 percent in addition to an automatic 1 percent that is contributed for all FERS, FERS-RAE, and FERS-FRAE 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 $19,500 and $19,000 of their salary to the thrift plan for the fiscal years ended September 30, 2020 and 2019, respectively, but with no automatic or matching amount contributed by FPI.

CSRS, FERS, FERS-RAE, and FERS-FRAE 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 $20,435 and $17,225 for the fiscal years ended September 30, 2020 and 2019, 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 $(26) and $1,612 in the fiscal years ended September 30, 2020 and 2019, 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 $7,531 and $6,828 for the fiscal years ended September 30, 2020 and 2019, 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 $5,137 and $4,302 during the fiscal years ended September 30, 2020 and 2019, 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.

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.

(Dollars in Thousands)

Note 10. Sales and Marketing, General and Administrative Expenses

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

Fiscal years ended September 30,	2020	2019
Salaries, wages and benefits	$ 28,703	$ 26,907
Permanent change of station expense	933	773
Purchases of minor equipment	995	367
Contract services	8,310	11,366
Bad debt expense	53	159
Credit card service fees	646	718
Travel	376	1,027
Personal computer expense	399	767
Accident compensation	(372)	2,701
Financial audit	1,497	1,310
Marketing	2,945	3,741
Depreciation	1,244	1,517
Loss on disposition of assets	47	16
Telecommunication expense	2,462	1,934
Other expense	571	1,361
Imputed pension costs	(26)	1,612
Imputed post-retirement health care and life insurance cost	5,137	4,302
Imputed operating costs	17,738	18,549
Sales and marketing, general and administrative expenses	$ 71,658	$ 79,127

Other expense is comprised primarily of gainsharing awards for staff and inmates, sales consulting fees, 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 $6.8 and $6.3 million for fiscal years 2020 and 2019, respectively. Contract services consist primarily of consulting and sales and marketing fees.

(Dollars in Thousands)

Note 11. 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. As of September 30, 2020 and 2019, legal contingencies total $0 and $600, respectively.

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, 2020 and 2019, future capital lease payments due total $8 and $37, and future operating lease commitments total $183 and $111, 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,***	**2020**	**2019**
Balance at the beginning of the period	$ 316	$ 327
Accruals for warranties issued during the period	19	201
Settlements made (in cash or in kind) during the period	(24)	(212)
Balance at the end of the period	$ 311	$ 316

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,	**2020**	**2019**
Congressional limitation on expenses	$ 2,700	$ 2,700
Expenses incurred subject to Congressional limitation	$ 2,277	$ 2,474