

• UNICOR OFFERS EXCEPTIONAL QUALITY PRODUCTS AND SERVICES: FURNITURE • OFFICE SYSTEMS • SEATING • CASEGOODS • DORMITORY PRODUCTS • COMPLEMENTARY PRODUCTS •

ELECTRONICS • CUSTOM MANUFACTURING & TESTING • ENVIRONMENTAL / CLIMATE PERFORMANCE EVALUATION • REMANUFACTURING OF VEHICLE PARTS • RECYCLED ELECTRONIC PRODUCTS & SERVICES • MOLDING • SOLDERING • BRAIDING

GRAPHICS / SIGNAGE • CREATIVE SERVICES • ARCHITECTURAL SIGNAGE • KIOSKS • GIFTS • RECOGNITION AWARDS • TEXTILES • MATTRESSES • APPAREL GARMENTS • CUSTOM APPLICATIONS • PERSONAL MAINTENANCE • SAFETY PRODUCTS

OF SERVICE TO OTHERS

UNICOR

2000 ANNUAL REPORT

• HYGIENE PRODUCTS • PRINTING • PRODUCTS & SERVICES • INDUSTRIAL / INSTITUTIONAL PRODUCTS • GROUNDSKEEPING • BUILDING MAINTENANCE & MANAGEMENT • STORAGE •

*It is the mission of Federal Prison Industries, Inc. (FPI) to...*

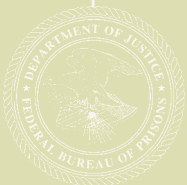
...Employ and provide job skills training to the greatest practicable number of inmates confined within the Federal Bureau of Prisons...

...Contribute to the safety and security of our federal correctional facilities by keeping inmates constructively occupied...

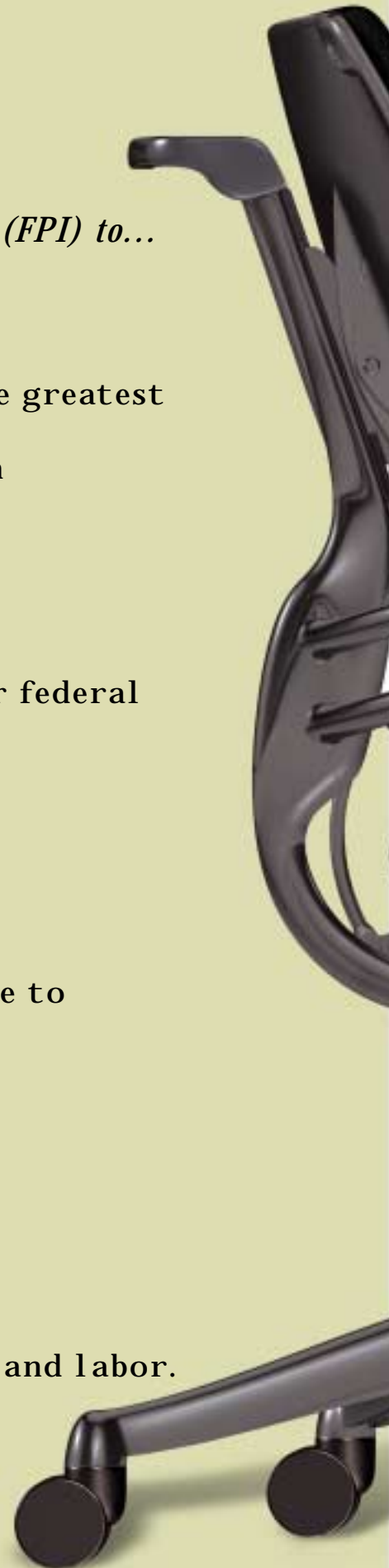
...Produce market-priced quality goods for sale to the Federal Government...

...Operate in a self-sustaining manner...

...And minimize FPI's impact on private business and labor.



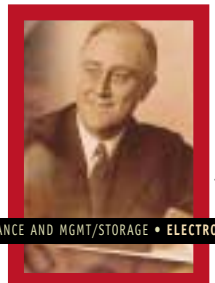
U.S. Department of Justice  
Federal Bureau of Prisons  
Federal Prison Industries, Inc.



## WHAT IS UNICOR?

**UNICOR** is the trade name of Federal Prison Industries, Inc. (FPI), a wholly-owned government corporation established by Congress on June 23, 1934, to provide job skills training and employment for inmates serving sentences in the Federal Bureau of Prisons.

*On December 11, 1934,  
President Franklin D. Roosevelt  
issued Executive Order No. 6917,  
which formally created  
Federal Prison Industries.  
FPI officially commenced  
operations on January 1, 1935.*



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**NET SALES (\$ MILLIONS)**

**Electronics \$133.9**



## FISCAL YEAR 2000 AT A GLANCE

### OPERATIONS HIGHLIGHTS

<i>(millions of dollars)</i>	1999	2000
Net Sales	\$ 566.2	\$546.3
Gross Profit	\$ 61.0	\$ 34.3
Net Income	\$ 16.6	-\$ 11.8
Purchases from Private Sector	\$ 423.4	\$410.7
Inmates Employed	20,966	21,688



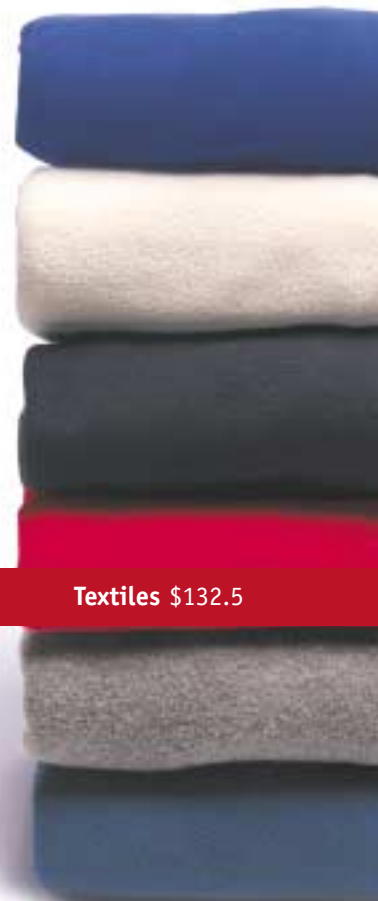
Furniture \$118.9



Graphics/Services \$51.9



Metals \$109.1



Textiles \$132.5

## AN INTRODUCTION BY THE ATTORNEY GENERAL

“What is our bottom line?” is a phrase commonly heard in corporate board rooms across America. Companies driven by profit simply want to know what their “bottom line” is at the end of the fiscal year. Were sales and earnings up or down for the year? Can we report a healthy profit to our shareholders? Although these are important questions to ask, for at least one corporation, Federal Prison Industries, Inc. (FPI), the true measure of success is reflected in the benefit to victims, savings to taxpayers, reduced crime, and lives changed.

We have all picked up papers from our local newsstands in the past 12 months to read attention-grabbing articles such as: *U.S. Prison Population Surpasses 2 Million* or *Number of Incarcerated First-Time, Non-Violent Drug Offenders Continues to Climb*. In the federal prison system alone, more than 145,000 inmates were incarcerated at the end of Fiscal Year 2000, and current projections indicate a rise to more than 200,000 by the end of Fiscal Year 2007. The fact is that 95 percent of those



ATTORNEY GENERAL JANET RENO

incarcerated in the Federal Bureau of Prisons will one day be released and return to our communities. If you and I expect them to become law-abiding, tax-paying citizens upon release, we have to support programs, such as FPI, that have proven to make a difference.

Federal Prison Industries (trade name UNICOR) is a wholly-owned government corporation that provides approximately 25 percent of the Federal Bureau of Prisons' sentenced inmate population with employment opportunities and job skills training. The program contributes daily to the effective management of our federal correctional facilities by keeping inmates constructively occupied. The inmates produce market-priced, quality goods for sale to the Federal Government. The program is self-sustaining and receives no appropriations for its operations. FPI's inmate workers are also required to contribute 50 percent of their wages to meet their financial obligations (family and court), thus reducing public assistance costs borne by the taxpayer.

What is even more encouraging is that a 16-year study of federal inmates (the Post-Release Employment Project) demonstrates convincingly that participation in prison industries/vocational training programs has a positive effect on post-release employment and recidivism. Specifically, the study revealed that inmates who worked in prison industries or completed

vocational and apprenticeship programs were 24 percent less likely to recidivate than non-program participants. The data also revealed that these programs provide even greater benefit to minority groups that are at the greatest risk for recidivism.

So as you can see, the "bottom line" for FPI is not about record-breaking profit levels. It is about being "**of service to others.**" For FPI, that means service to you as a taxpayer and citizen, to our federal correctional system, to FPI's customers and partners, and to victims of crime. The "bottom line" is about changing the lives of offenders so that they have the chance to become responsible, contributing individuals in society.



Janet Reno

## A JOINT MESSAGE FROM THE FPI BOARD OF DIRECTORS AND CHIEF EXECUTIVE OFFICER

Federal Prison Industries' Board of Directors and Chief Executive Officer are proud to present FPI's Fiscal Year (FY) 2000 Annual Report to the Congress of the United States. This year's report, titled "UNICOR: Of Service to Others," focuses on what being "of service" means to each of FPI's constituents.

By statute, FPI is a mandatory source provider of a wide array of products to the Federal Government, yet we firmly believe that by offering competitive prices and quality products/innovations responsive to federal customers' needs, agencies will freely support FPI's mission without feeling compelled to do so.

The Attorney General mentioned in her introductory remarks, "FPI is not about record-breaking profit levels. It is about being 'of service to others.'" *Webster's Dictionary* defines "service" as: "(1) a contribution to the welfare of others; and (2) an array of activities which enhances the value and enjoyment of the items/services obtained." So you may ask what "service" and the running of a correctional industries program have in common? The answer is simple — everything!



OFFICE ACCESSORIES

One in every 250 adult residents in the United States is serving a prison/jail sentence of a year or more. Sadly, the trend is spiraling upward faster than our Nation can build correctional facilities to respond. The vast majority of offenders eventually return to our communities after serving their terms. Wouldn't we prefer that offenders learn meaningful skills or trades, and develop a positive work ethic while incarcerated?

FPI's program serves society by making prisons safer and less costly to operate, and by helping offenders reform their behaviors so their prospects of becoming legitimately employed members of our society are improved. The antithesis of FPI's program — to lock up prisoners and throw away the key — is no way to solve this country's crime problem.

Unlike most Federal Government programs, FPI does not rely on taxpayer dollars to maintain its operations. Instead, revenue to pay staff salaries, run factory operations, and support the program is generated by the sale of products and services.

The degree to which FPI meets its federal customers' expectations not only directly impacts the program's overall success, but also has a rippling effect on virtually everyone:

- **Federal customers** benefit from FPI's competitive product and service offerings and streamlined procurement procedures.
- **The private sector** benefits because employers are more receptive than ever to hiring ex-offenders who have marketable job skills and are motivated to work. Low unemployment rates have

businesses scrambling for qualified workers like never before. Initiatives, such as the Bureau of Prisons' Inmate Placement Program, have been a resounding success to help inmates hone their job interviewing skills and to promote the positive changes they have made in their lives while incarcerated.

- **Local businesses** benefit financially from FPI's purchases to support its production operations. During FY 2000, FPI spent approximately \$410



CASEGOODS/WOOD LAMINATE

million on the purchase of raw materials, supplies, equipment, and services. As a federal agency, FPI actively supports small businesses through its procurements, and awarded 63 percent of its procurements to small businesses, including small, women/minority-owned, and disadvantaged businesses.

- ***The Federal Bureau of Prisons*** benefits from the added staff safety and prison security that is inherent in keeping inmates productively occupied. Research studies have shown that inmates who participate in vocational training and work programs are less likely to engage in institutional misconduct.
- ***Inmates' families and crime victims*** benefit from the monetary support and restitution inmates provide from their job earnings. Inmates who work in FPI factories are required to pay at least 50 percent of their earnings to meet financial obligations such as court-ordered fines, child support, and/or

restitution. During FY 2000, FPI inmate workers paid \$2.5 million toward these obligations.

- ***Thousands of incarcerated men and women in our Nation's correctional facilities*** benefit because FPI represents a "second chance." The late Chief Justice Warren Burger often extolled the merits of "factories with fences," and recognized the need to balance the interests of private industry with correctional goals. He firmly believed that the key ingredient in reducing recidivism was instilling a strong work ethic in inmates. Studies confirm that inmates who have gained job experience working in FPI factories are more likely to become law-abiding, employed citizens making positive contributions to society.
- ***We and our communities*** benefit from safer neighborhoods, thanks to the reintegration of men and women who become gainfully employed taxpayers upon release from prison.



OFFICE SYSTEMS

## WELCOME TO FPI'S NEWEST BOARD MEMBER

DEIDRE A. LEE

Federal Prison Industries is pleased to announce the appointment of Deidre A. Lee to FPI's Board of Directors. On June 23, 2000, President Clinton named Ms. Lee to FPI's Board of Directors, filling the Secretary of Defense seat vacated by former Board Member Todd Weiler.



Ms. Lee, of Arlington, Virginia, has served as the Director of Defense Procurement in the Department of Defense since June 2000. From August 1998 to May 2000, she served as Administrator of the Office of Federal Procurement Policy. Prior to that position, Ms. Lee was the Associate Administrator for Procurement and the senior acquisition official at the National Aeronautics and Space Administration (NASA). During her time at NASA, Ms. Lee was responsible for a number of successful procurement initiatives, and she was awarded NASA's Outstanding Leadership Medal and the Exceptional Achievement Medal for her many accomplishments. In 1996, she received the Senior Executive Service Presidential Rank Award. Ms. Lee earned her Bachelor of Arts degree from Central State University of Oklahoma and her Master's in Public Administration from the University of Oklahoma. Her insight, from a customer's perspective, and her knowledge of procurement policy will be invaluable as the corporation strives to be "of service" to those who purchase our products and/or services.

FPI must vie for its customers' procurement dollars as would any supplier, mandatory source notwithstanding. This means constantly searching for the types of efficiencies, conveniences, and innovations of key importance to federal customers. This is a continually evolving process because what makes us good enough to earn a customer's support today will not necessarily be good enough to sustain it tomorrow.

FPI continues to position itself for future success. Its mission as a correctional program is simply too critical to be compromised or abandoned. During FY 2000, a number of initiatives were launched, all of which were

implemented to significantly improve FPI's ability to manage its day-to-day operations, strategically plan ahead, and offer federal customers the caliber and range of improved services and attention necessary to preserve their support.

As you read in this report about some of FPI's corporate-wide, service-inspired initiatives, we ask that you keep in mind the complexity of this corporation's mission and the delicate balance it must achieve to serve all of its constituents.



ELECTRONICS

## MAINTAINING THE DELICATE BALANCE

It is said that everything in life is a tradeoff. Every choice taken precludes an alternative choice. You really cannot have your cake and eat it too. Nowhere is this more true than with the various public policy choices associated with Federal Prison Industries.

FPI has multiple and often conflicting mandates reflecting the varied interests of its constituents. As FPI strives to meet these mandates and to be of service to its constituents, it must maintain a delicate balance between its mission as both a business and a correctional program.

FPI is required to employ as many inmate workers as practicable, diversify its production to minimize the impact on any particular segment of private industry, teach inmates marketable skills, and be financially self-sufficient. The challenge of operating FPI under these mandates is complicated by the burgeoning federal inmate population, which is projected to

increase by 40 percent in the next seven years. This population increase and the corresponding growth in FPI present a number of challenges and tradeoffs that must be considered. For example:

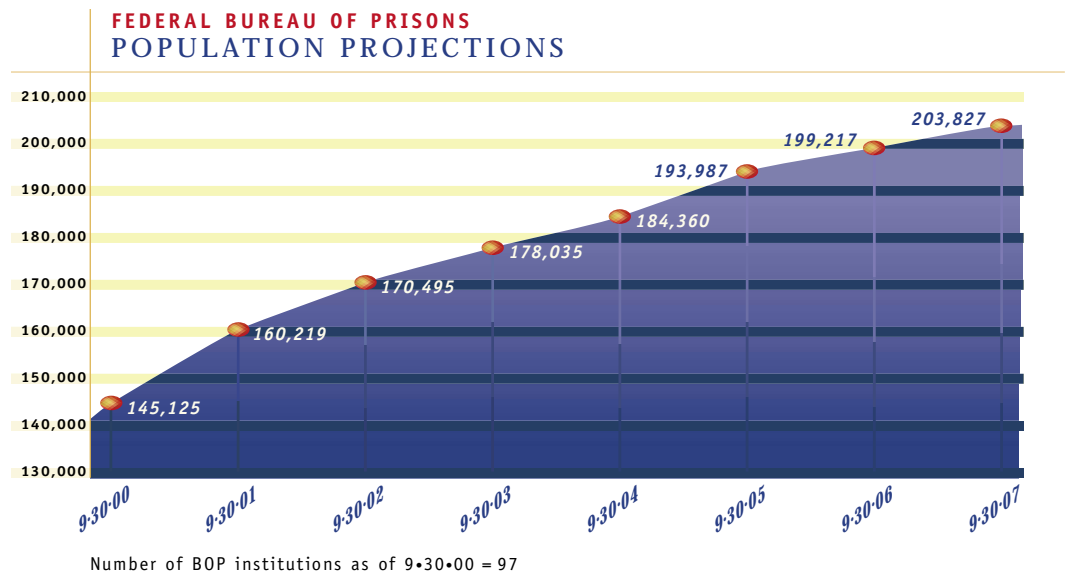
- To maximize inmate employment, the work must be as labor intensive as possible. This typically leads to the use of less modern production methods and equipment as opposed to the private sector trend toward automation. However, the more labor intensive approach conflicts with the mandate of teaching inmates skills that are directly comparable to those in the private sector. What is the appropriate balance between these two alternatives?
- Adverse impact on the private sector can be minimized by diversifying production among numerous product lines. This diversification, however, results in smaller production runs and lower efficiencies. The resulting increase in costs makes it even more challenging to be financially self-sustaining. Assuming that the private sector will generally oppose any growth in FPI's production, is it more appropriate for FPI to increase its production of existing product lines or diversify into new industries where FPI does not currently compete?

*Metal Shelving Production Factory*

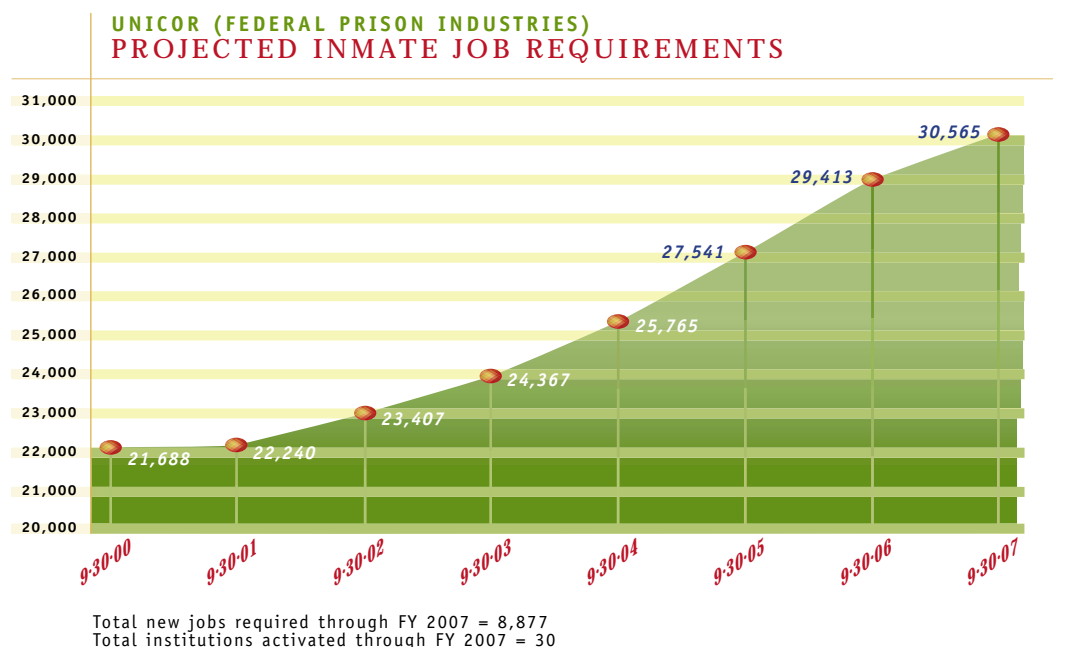


INDUSTRIAL/INSTITUTIONAL PRODUCTS

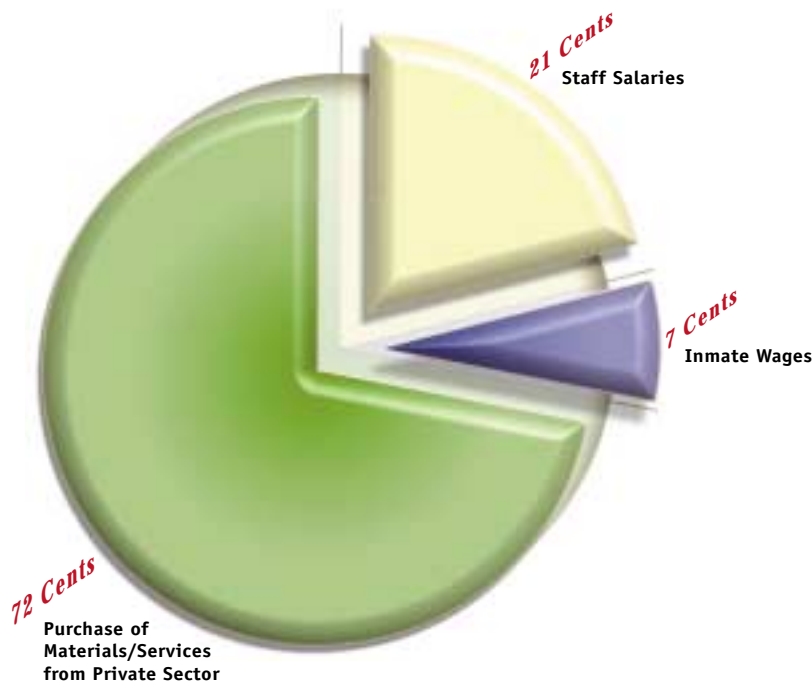
- One way to avoid adverse impact on private sector workers is to have inmates perform tasks that cannot be economically performed domestically, i.e., providing products or services that are currently imported or provided by foreign countries. Again, this conflicts with the mandate of teaching marketable skills since they will be involved in operations not currently performed in the United States.



- Inmates working in FPI who have court-ordered fines, child support, and victim restitution are required to pay 50 percent of their earnings toward these financial obligations. If FPI were to operate in a more real-world manner by paying inmates higher earnings, more money could be collected toward these obligations. However, for FPI to absorb the higher costs resulting from a wage increase, it would be necessary to increase total production or employ fewer inmates.



## HOW EACH FPI DOLLAR IS EXPENDED



- Comprehensive professional research demonstrates conclusively that inmates who work in FPI and participate in vocational training present fewer disciplinary problems while incarcerated and are much more likely to obtain employment and remain law-abiding citizens upon release. FPI currently has a goal of employing 25 percent of the work-eligible inmate population. Given the proven benefits of participation in FPI, should this goal be higher? As the inmate population continues its relentless increase, the number of inmates employed in FPI is also expected to rise. Is there a point at which the inmate employment goal should be reduced to minimize the impact on the private sector? What implications does this have for inmate idleness and its effect on safe prison management? What is the proper balance between the proven societal and correctional benefits of FPI and the impact on private sector business?

The operation of a prison industries program epitomizes the complexity of public policy choices. Many constituents exist: private sector companies and workers, crime victims, prison staff, judges, prosecutors, inmates and their families, and the communities in which the prisons reside. Each has legitimate, but often competing and conflicting, interests that are intertwined in FPI's statute. No easy answers exist and addressing each interest requires tradeoffs. The more sensitive and numerous the tradeoffs, the more challenging it is to **maintain the delicate balance.**

## UNICOR: A LIFESAVER



Border Patrol Agent Michael Smith, while inspecting a vandalized generator light last August along the international boundary near Calexico, California, heard a sharp popping sound and felt a strong impact on his back.

Believing he was a victim of a rock assault, Agent Smith turned to search for his assailant, but no one was in sight. He drove to a safe location and proceeded to inspect the area

where he was hit. To Agent Smith's amazement, apart from the small hole in his shirt, he discovered a small caliber bullet lodged in the Kevlar lining of his UNICOR ballistic vest. Agent Smith only received a small welt at the site of impact. Had he not been wearing a quality vest, however, the outcome of the assault might have been much different.

A grateful Agent Smith was inducted into the International Association of Chiefs of Police (IACP)/DuPont Kevlar Survivors' Club on November 12, 2000. UNICOR's Program Manager for body armor looked on with pride because, thanks to the inmate workers at the Federal Correctional Institution in Bastrop, Texas, he was keenly aware of the crucial role they played in producing a quality safety vest responsible for achieving such a "happy ending."



LAW ENFORCEMENT PRODUCTS

## A SUCCESSFUL TRANSITION

### *Ex-offender Is on the Right Track to Success*

Ex-offenders who return to society after years or decades of incarceration are faced with an uphill challenge to successfully reintegrate into the world. They are often overwhelmed by the changes in society and in the job market. Despite record-low unemployment levels and jobs that remain perpetually “open,” many employers have policies that prohibit the employment of individuals having criminal records. Others are reluctant to “take a chance” and risk adverse reactions from their employees, customers, or the public by hiring ex-offenders. Yet, the benefits to society are immeasurable when ex-offenders find worthwhile employment and become law-abiding citizens.

Federal Prison Industries provides more than the basic fundamentals for reducing recidivism. It goes a step further in conjunction with the Bureau of Prisons’ Inmate Placement Program. This program, in partnership with volunteers from the academic and private sectors, teaches inmates resumé writing, job

seeking, and employment interviewing skills by sponsoring mock job fairs at federal correctional institutions across the country. The aim of the program is to improve the prospects for ex-offenders to find meaningful employment.

Ultimately, society wins when ex-offenders become positive role models, pay taxes, no longer resort to crime, and do not return to prison. Just ask Bill Drayer for his perspective. Mr. Drayer has “been there and done that.”

Mr. Drayer, a former inmate at the Federal Correctional Institution (FCI), Allenwood, Pennsylvania, possessing a positive attitude, drive to succeed, and marketable job skills, re-entered the job market. Mr. Drayer staunchly believes in the “I think I can” philosophy. It is an attitude that has elevated him to his present success.

Recently, Mr. Drayer was hired by Blockhouse, an industry leader in the college and military furniture market, located in York, Pennsylvania. It was an ideal match.

Mr. Drayer had always enjoyed working with wood and Blockhouse is recognized for its high quality product, which particularly attracted him.

At Blockhouse, Mr. Drayer constructively applied his woodworking skills and furniture production knowledge gained from

DORM AND QUARTERS FURNITURE



*Bill Drayer and Blockhouse CEO John Brown*

on-the-job factory experience while incarcerated. While working in the UNICOR factory in Allenwood, Mr. Drayer actually performed woodworking in support of a contract between FPI and Blockhouse. So, when he started looking for work, Blockhouse was the perfect choice for employment; it was close to home and he was already qualified for the job.

Blockhouse is just one of the many companies currently tapping into a labor pool previously considered untouchable: ex-offenders. With the current low unemployment rate, more private sector companies are posting “help wanted” signs in halfway houses and participating in prison job fairs to recruit ex-offenders. This is a marked shift from a few years ago

when ex-offenders struggled just to get interviews. The Federal Bureau of Prisons, in addition to many state corrections departments, have stepped up their inmate training programs to help prisoners gain marketable job skills in order to assist them upon release.

Mr. Drayer is an upholsterer in Blockhouse’s Upholstery Department. Before his release from prison, Mr. Drayer said his greatest fear was not finding employment because of his age and his felony conviction. He never imagined that he would find a job he enjoyed and an employer for whom he would be proud to work. Mr. Drayer says his personal goals are “to get to work on time, work hard, and never miss a day of work. Follow that creed, and everything else will fall into place.”

Of course, hiring Mr. Drayer has also been good for Blockhouse. According to the firm’s CEO, John Brown, “Mr. Drayer is dedicated to putting out a quality product on time, is a team player, and is well liked by his co-workers. His positive attitude rubs off on others. More importantly, Mr. Drayer has lived up to his own goals — he has never been late for work and he has never missed a day of work.”

Mr. Drayer also has another goal: to help Blockhouse in any way he can because Blockhouse was willing to give *him* a second chance. This is good news to Blockhouse. In view of the company’s success in hiring ex-offenders, CEO John Brown says “Blockhouse would love to hire 100 Bill Drayers.”

## CUSTOMER SERVICE IS MORE THAN PROCESSING AN ORDER

Customer service expectations in today's society have never been higher. Long gone are the days when customer service simply meant a friendly voice taking your order over the phone and your product or service being delivered at some future date. With the advent of fax machines, express mail, and the Internet, customers have become accustomed to getting what they want, often within 24 hours, hassle free.

Being "of service" in today's world *is more than processing* an order — it's about...

- *having a dynamic and knowledgeable sales and marketing force*
- *making it easy and expedient for the customer to place and track orders*

• LISTENING TO  
WHAT  
CUSTOMERS  
WANT

• being

- meeting the customer's performance expectations

Testing New Products



PRODUCT SUPPORT CENTER



RECOGNITION AWARDS

- a willingness to “re-engineer” one’s corporation to meet ever-changing customer demands

• **ON-TIME  
DELIVERY OF  
PRODUCTS  
AND/OR  
SERVICES**

# innovative

• personal  
follow-up

• product expansion

• *a reputation based on proven ability to satisfy customer needs*

• **PARTNERSHIPS**

FPI customer expectations are certainly no less demanding.

Following are several articles that demonstrate FPI’s commitment to customer service. Many are new initiatives that will enhance FPI’s ability to be “of service” to you.

## NEW BUSINESS PROCESS AIMED AT ACHIEVING SERVICE EXCELLENCE

On May 30, 2000, Federal Prison Industries launched an Enterprise Resource Planning (ERP) system to replace its existing manufacturing database. The new ERP system, called Millennium, is the first major redesign of UNICOR's computer system in more than a decade and will significantly change how the corporation manages its day-to-day operations and how it plans for the future.

Constrained by the parameters of the old system, FPI staff set out in search of an "off-the-shelf solution" more closely aligned with the corporation's current business processes. Ultimately, FPI purchased SAP (Systems, Applications, Products in Data Processing) to replace its existing manufacturing database.

The new centralized system is used to control order entry, factory loading, production scheduling, vendor purchases, project management, cost accounting, financial reporting, delivery, logistics scheduling, and customer feedback. The system is capable of supporting 3,000 total users, 1,500 of them simultaneously. It serves

100 different factories and a diverse product and service line. Millennium provides UNICOR managers with real time data on all operating aspects of the corporation, facilitating their ability to make timely and well informed decisions based on the most current information available. The end result: (1) improved production scheduling; (2) reduced inventory and procurement costs; (3) faster and more accurate financial data; and (4) improved customer service.

Although the new system will eventually make FPI operations more efficient, candidly, its implementation proved to be much more demanding than anticipated. Because of operational impacts resulting from the new system implementation, including but not limited to, decreased sales, increased loss reserves, and reallocation of resources, the corporation experienced a loss of \$11.8 million for the fiscal year ended September 30, 2000. Further, in connection with our FY 2000 financial statement audit, our independent auditors identified systemic and internal control deficiencies associated with inventory valuation, accounts receivable management, and cash management. These matters, among others, contributed to an audit qualification on our FY 2000 financial statements. FPI staff have developed a corrective action plan to address each noted deficiency. It is the goal of the Board and the staff to return to positive earnings and an unqualified audit opinion in FY 2001.



- a willingness to "re-engineer" one's corporation to meet ever-changing customer demands

# millennium

# ● *being innovative*

## INDUSTRIAL PROGRAMS, LOCATIONS, INMATE EMPLOYMENT, AND NET SALES AS OF SEPTEMBER 2000

Textiles	Electronics	Furniture	Metals	Graphics/Services
<ul style="list-style-type: none"> <li>■ Alderson, WV</li> <li>■ Atlanta, GA</li> <li>■ Beaumont, TX</li> <li>■ Butner, NC</li> <li>■ Dublin, CA</li> <li>■ Edgefield, SC</li> <li>■ Fort Dix, NJ</li> <li>■ Greenville, IL</li> <li>■ Jesup, GA</li> <li>■ Leavenworth, KS</li> <li>■ Manchester, KY</li> <li>■ Miami, FL</li> <li>■ Oakdale, LA</li> <li>■ Otisville, NY</li> <li>■ Ray Brook, NY</li> <li>■ Safford, AZ</li> <li>■ Sandstone, MN</li> <li>■ Seagoville, TX</li> <li>■ Terre Haute, IN</li> <li>■ Tucson, AZ</li> <li>■ Waseca, MN</li> <li>■ Yazoo City, MS</li> </ul>	<ul style="list-style-type: none"> <li>■ Bastrop, TX</li> <li>■ Beaumont, TX</li> <li>■ Big Spring, TX</li> <li>■ Danbury, CT</li> <li>■ Estill, SC</li> <li>■ Fairton, NJ</li> <li>■ Lexington, KY</li> <li>■ Lompoc, CA</li> <li>■ Loretto, PA</li> <li>■ Marion, IL</li> <li>■ Memphis, TN</li> <li>■ Oxford, WI</li> <li>■ Petersburg, VA</li> <li>■ Phoenix, AZ</li> <li>■ Rochester, MN</li> <li>■ Three Rivers, TX</li> <li>■ Victorville, CA</li> </ul>	<ul style="list-style-type: none"> <li>■ Allenwood, PA</li> <li>■ Ashland, KY</li> <li>■ Beckley, WV</li> <li>■ Dublin, CA</li> <li>■ Florence, CO</li> <li>■ Forrest City, AR</li> <li>■ Leavenworth, KS</li> <li>■ Lompoc, CA</li> <li>■ Marianna, FL</li> <li>■ Sheridan, OR</li> <li>■ Taft, CA</li> <li>■ Talladega, AL</li> <li>■ Tallahassee, FL</li> <li>■ Texarkana, TX</li> </ul>	<ul style="list-style-type: none"> <li>■ Coleman, FL</li> <li>■ El Reno, OK</li> <li>■ Lewisburg, PA</li> <li>■ McKean, PA</li> <li>■ Milan, MI</li> <li>■ Morgantown, WV</li> <li>■ Pekin, IL</li> <li>■ Schuylkill, PA</li> <li>■ Terminal Island, CA</li> </ul>	<ul style="list-style-type: none"> <li>■ Bryan, TX</li> <li>■ Butner, NC</li> <li>■ Carswell, TX</li> <li>■ Cumberland, MD</li> <li>■ Dublin, CA</li> <li>■ Eglin, FL</li> <li>■ El Paso, TX</li> <li>■ Elkton, OH</li> <li>■ Fort Dix, NJ</li> <li>■ Fort Worth, TX</li> <li>■ La Tuna, TX</li> <li>■ Leavenworth, KS</li> <li>■ Lexington, KY</li> <li>■ Lompoc, CA</li> <li>■ Marianna, FL</li> <li>■ Montgomery, AL</li> <li>■ Petersburg, VA</li> <li>■ Sandstone, MN</li> <li>■ Taft, CA</li> <li>■ Tallahassee, FL</li> </ul>
<b>Inmates Employed:†</b>				
6,540	3,959	4,671	3,443	3,075
<b>Net Sales:*</b>				
\$132.5	\$133.9	\$118.9	\$109.1	\$51.9

Some locations have multiple plants.

† The total number of inmates employed by Federal Prison Industries as of **September 2000** was **21,688**.

This includes **2,924** inmates employed in support positions.

\* Dollars in millions

GIFTS



## • LISTENING TO WHAT CUSTOMERS WANT

### “YOUR WAY” OF DOING BUSINESS

FPI, commonly referred to by its trade name UNICOR, wants to be the government’s first choice of supply and to earn this distinction, it recognizes that ordering must be easy, delivery must be expedient, products must be competitive, and quality must meet customers’ expectations. Hand-in-hand with these requirements is UNICOR’s unwavering commitment to research and implement new technologies that will further enhance its value to customers in all of these areas. At UNICOR, we want to do things *your* way, not ours, so that you will remain a dedicated supporter.

UNICOR is listening and reacting to what customers are asking. Surveys are conducted regularly to obtain your thoughts about the types of expedited services customers find critical, and how well UNICOR is performing in general. Based on this invaluable feedback, a number of customer service based improvements occurred in FY 2000, which we are pleased to share.

#### • *We’re just a “click” away*

The Internet has changed the manner and speed in which the world does business, and UNICOR rose to

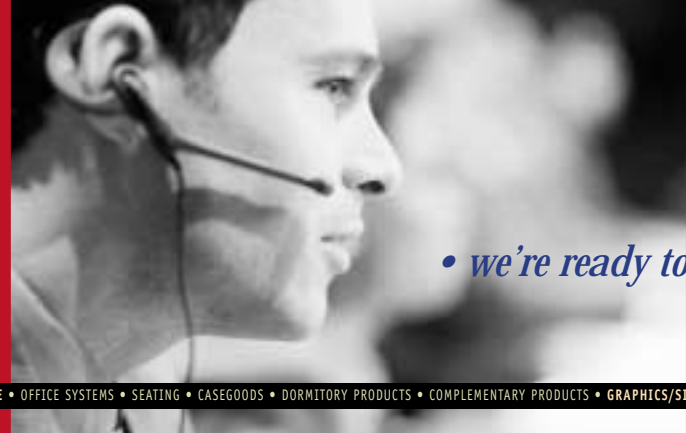
the challenge by creating an award-winning website where customers can browse through its many products and services, place on-line orders, check order status, locate their local sales representatives, learn about upcoming trade shows, and even request waivers. Customers can also express concerns they have about UNICOR products, services, and customer service levels on-line. All input is monitored closely to identify potential problem areas in need of attention.

#### • TALK TO US

UNICOR’s Customer Service Center is undergoing constant improvements to service customers better, whether through the toll-free hot line or operational changes to enhance overall service levels. Recently, FPI installed a new computer system to improve telephone responsiveness. FPI also added staff to provide additional credit card order coverage. The Customer Service Center also entered into a national shipping/logistics contract to ensure on-time delivery of your orders. In response to customers’ requests for consolidated billing statements, we centralized UNICOR’s billing function to do just that.

Some customers have technical information needs above and beyond what the Customer Service Center’s telephone agents can provide. In response, FPI created a technical help desk, staffed by UNICOR engineers

Customer Service



• *we’re ready to help — near or far*

- *making it easy and expedient for the customer to place and track orders*

and other specialists, to provide answers to customers' questions about matters concerning product design, specifications, safe use, and capability, as well as care and maintenance of UNICOR products.

- *Staying one step ahead*

After initiating a corporate-wide process improvement initiative, UNICOR determined that it needed to concentrate more focus on project management activities to coordinate more effectively deliveries of furniture products and the logistics of federal facility projects. Accordingly, FPI created a new project management group to serve as the "air traffic controllers" for all UNICOR orders involving multiple factory shipments. Staff plan and coordinate work activities, establish a critical path for the production and shipment of products, manage project execution time lines, and keep customers informed throughout the entire planning and implementation processes. Group members are also customer advocates, who do whatever is necessary to ensure the timely completion of complex projects to the complete satisfaction of our customers.

- *We're ready to help — near or far*

In an ongoing effort to enhance its level of customer service in the office furniture products area (which accounts for a significant portion of UNICOR's sales), UNICOR established a support service agreement in FY 2000 with Government Marketing Group (GMG),

a commercial firm, to exclusively sell and service UNICOR office furniture products. GMG is staffed by sales professionals whose educational backgrounds and work experience in the design and furniture industry are extensive. With the introduction of GMG, UNICOR can offer customers a single point of contact to meet all their needs. Coverage was expanded from four regions to a total of 13, to include Hawaii, thereby increasing UNICOR's accessibility to customers.

UNICOR also recognized a need to provide heightened levels of expertise in conjunction with project-level procurements. An exciting new program, known as the *Select Program*, was recently offered to both military and civilian agencies. The program provides more latitude for agencies to determine when, where, and to what degree UNICOR items are to be used for their current and prospective facility projects. The *Select Program* essentially enables federal designers, on behalf of their agencies, to fulfill a portion of their project needs through UNICOR, while providing automatic waiver approval for other items/projects so they can be procured through outside sources.

UNICOR will continue to explore new avenues to help it offer customers expedited and enhanced services and will pay particular attention to listening and responding to customers' expressed needs.

- *having a dynamic and knowledgeable sales and marketing force*

being innovative

ELECTRONICS



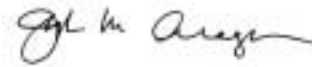
## THE QUEST AHEAD

FPI began its operations during the economic depression in the 1930s. It became a major defense supplier during World War II. From producing canvas feedbags and wicker settees during its early years to offering more than 150 diverse products and services today, FPI has adapted, enhanced, and widened its product lines in response to its federal customers' changing needs. Although much has changed during this transition, FPI has maintained an unwavering commitment to customer service and to its goal of helping our Nation's law enforcement efforts by making a positive impact in inmates' lives.

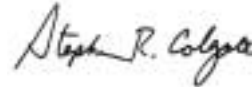
Good customer service means giving people what they need, which is a long-term investment in change. To determine what customers want requires effective information systems to measure and assess service levels, a dedicated, responsive staff to develop and nurture ongoing customer relationships, and a corporate culture focused on quality at every level of the organization. FPI embodies all of these elements

and continues to explore innovative production methods and technological improvements to add value to the products and services it provides to its customer base. Although many initiatives were highlighted in this year's Annual Report, there is not enough room to share all that FPI is undertaking to cultivate its customer, private sector, business partner, and vendor relationships.

FPI has done an outstanding job of being "of service" to others for the past 65 years and we look forward to serving you, the reader, whatever your interests, well into the new Millennium.



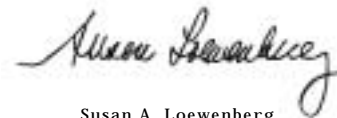
Joseph M. Aragon



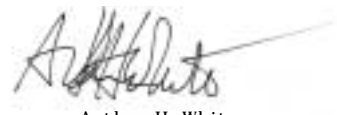
Stephen R. Colgate



Deidre A. Lee



Susan A. Loewenberg



Arthur H. White



Richard G. Womack



UNICOR ONLINE



## REPORT FROM THE OMBUDSMAN

The words *mandatory source* and *waivers* are viewed as uncomfortably negative subjects when brought up in FPI procurement discussions. When UNICOR's waiver activity is reported each year, the dollar figures seem to conjure up visions of sales that UNICOR "captured" (denied waivers) versus those that "escaped" its clutches (approved waivers), and were ultimately "rescued" by the private sector (non-UNICOR sales). Sadly, a perception exists that UNICOR thinks nothing of sacrificing customer satisfaction for the greater good of its program. But nothing could be further from the truth.

UNICOR's mandatory source provision helps it maintain inmate employment levels and ensures a steady flow of business from the federal market. However, FPI cannot meet every customer's demands and consequently it instituted a formal policy for waiving its mandatory source. UNICOR has since relinquished anywhere from 80 percent to 94 percent of potential sales over the years by approving waiver requests, out of deference to its federal customers' needs.

UNICOR carefully considers the customer's requirements and assesses whether it offers products that will satisfy them before issuing a decision to approve or deny the waiver. An appeal process exists should the customer wish to challenge a waiver denial,

and the customer may likewise further elevate the matter through an independent, statutorily appointed Waiver Review Panel for a final, binding decision. The waiver process is simple and

expeditious. It can even be initiated on-line through UNICOR's website.

UNICOR differs from a traditional business in that its projected sales objectives correlate to the numbers of employable inmates in federal custody. If incarceration levels were to drop dramatically, UNICOR's sales objectives would follow suit. In the private sector, sales objectives are focused in a single direction: upward. So, you might say that UNICOR is not competitive in the sense of going after sales to grow the corporation, but rather it provides federal customers products and services to achieve its programmatic responsibilities.

During FY 2000, UNICOR received 19,464 requests to waive its mandatory source, representing a record \$513.5 million in potential sales, the majority of which were for office furniture products. In some cases, UNICOR was unable to meet customers' delivery requirements. In other cases, it could not meet certain technical requirements or other critical specifications. As such, UNICOR approved 82 percent of the waiver dollars, resulting in \$420.3 million being diverted to the private sector. Nearly half of the waivers denied were appealed, and for various reasons 79 percent of the appeals were granted. This represented an additional \$36 million in sales for the private sector. Net/net, of the \$513.5 million in potential waiver-related sales UNICOR could have obtained had its mandatory source provision been truly "mandatory," UNICOR retained only \$57.2 million (11 percent) and redirected the balance of \$456.3 million to the private sector. I cannot think of a more graphic way to demonstrate the extent to which UNICOR is committed to its customers.

Jan I. Hynson, Ombudsman



## YOU HAVE A DIRECT LINE . . .

### *How to Contact FPI's Board of Directors*

If you have a question or concern you would like addressed by FPI's Board of Directors, you may contact any one of the members at his/her respective business address listed below:



**Joseph M. Aragon, Chairman**  
President, ProServe Corporation  
730 17th St, #817  
Denver, CO 80202

**Represents Retailers and Consumers**



**Arthur H. White, Vice Chairman**  
Vice Chairman, Yankelovich Partners, Inc.  
101 Merritt 7 Corporate Park  
Norwalk, CT 06851

**Represents Agriculture**



**Stephen R. Colgate**  
Assistant Attorney General  
for Administration  
U.S. Department of Justice  
950 Pennsylvania Ave., NW, Room 1111  
Washington, DC 20530

**Represents the Attorney General**

**Deidre A. Lee**

Director, Defense Procurement  
3060 Defense Pentagon, Room 3E144  
Washington, DC 20301-3060

**Represents the Secretary of Defense**



**Susan A. Loewenberg**  
Producing Director, L.A. Theatre Works  
681 Venice Boulevard  
Venice, CA 90291

**Represents Industry**



**Richard G. Womack**  
Director, Office of Civil Rights  
AFL-CIO  
815 16th St. NW, Room 410  
Washington, DC 20006

**Represents Labor**



or you may direct your inquiries to Federal Prison Industries, Inc., 320 First St., NW, Washington, DC 20534, Attention: Joseph M. Aragon, Chairman, Board of Directors, Federal Prison Industries, Inc.

FPI's Board of Directors is pleased to announce that, beginning in Spring 2001, FPI's website will be expanded to include links to information concerning future Board meetings, Public Notices, and Board Decisions. In addition, persons interested in addressing the Board at one of its regularly scheduled meetings in Washington, DC, may forward their requests to Chairman Aragon for consideration.

## REPORT OF MANAGEMENT

Responsibility for the integrity and objectivity of the financial information in this report rests with the management of Federal Prison Industries, Inc. The accompanying financial statements have been prepared to conform with generally accepted accounting principles.

To ensure the integrity of financial data, FPI management maintains a system of internal accounting controls. The system provides reasonable assurance that transactions have management authorization and are properly recorded. It also safeguards, verifies, and maintains accountability of assets and permits preparation of financial statements that conform with generally accepted accounting principles. This system of internal controls is subject to periodic reviews by both management and FPI's independent auditors.

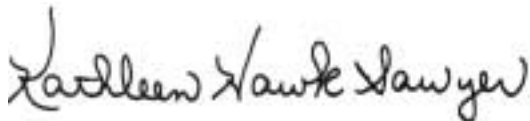
Internal accounting and administrative control systems have been reviewed and tested. Accordingly, FPI management provides the following assurances:

1. There are sufficient controls and security measures to compensate for any identified risks associated with the program/system and/or its environment,
2. The program/system is being operated in an effective manner and complies with applicable laws and regulations,
3. There is proper management of the program/system information, and
4. The program/system complies with management, financial, information resources management, accounting, budget and other appropriate standards.

The independent certified public accounting auditing firm of Urbach Kahn & Werlin PC is retained to audit FPI's financial statements. The role of independent auditors is to provide an objective review of management's responsibilities to fairly report operating results, cash flows and financial position. The independent auditor's reports are presented on the following pages. The report on the fairness of the presentation of the FY 2000 financial statements is qualified.

The independent auditor obtains an understanding of FPI's internal control structure sufficient to plan the audit and to determine the nature, timing, and extent of tests to be performed to form an opinion on the fairness of the presentation of the financial statements.

Management has developed, in cooperation with our independent auditors and the Office of Inspector General, a corrective action plan to address concerns noted in the Internal Control Reports. As implemented, these actions will further strengthen FPI's system of internal controls.



Kathleen Hawk Sawyer  
*Director, Federal Bureau of Prisons*  
*Chief Executive Officer, Federal Prison Industries*

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***Independent Auditor's Report on the Financial Statements***

Office of the Inspector General  
United States Department of Justice

Board of Directors  
Federal Prison Industries, Inc.

We have audited the accompanying Balance Sheets of Federal Prison Industries, Inc. (FPI), a bureau of the United States Department of Justice, as of September 30, 2000 and 1999, and the related Statements of Operations and Cumulative Results of Operations, and Cash Flows for the years then ended. These financial statements are the responsibility of the management of FPI. Our responsibility is to express an opinion on these financial statements based on our audits.

Except as discussed in the following paragraph, we conducted our audits 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 Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

Because of costing errors identified in certain inventory records, we were unable to sufficiently extend our auditing procedures to the work-in-process and finished sub-assembly components of inventories at September 30, 2000, stated at \$19.8 million and \$11.7 million, respectively (Note 4 to the financial statements). Accordingly, we were unable to form an opinion regarding the amounts at which these components are carried in the accompanying balance sheet as of that date, or the related effect on cost of sales for the year then ended.

In our opinion, except for the effects on the 2000 financial statements of such adjustments, if any, as might have been determined to be necessary had we been able to sufficiently extend our auditing procedures as discussed in the preceding paragraph, the financial statements referred to in the first paragraph above present fairly, in all material respects, the financial position of Federal Prison Industries, Inc. as of September 30, 2000 and 1999, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued reports dated January 5, 2001 on our consideration of FPI's internal control over financial reporting, and on our tests of its compliance with certain provisions of applicable laws and regulations. These reports are an integral part of an audit performed in accordance with *Government Auditing Standards*, and in considering the results of the audit, these reports should be read in conjunction with this report.



Washington, DC  
January 5, 2001

### ***Independent Auditor's Report on Internal Control***

Office of the Inspector General  
United States Department of Justice

Board of Directors  
Federal Prison Industries, Inc.

We have audited the financial statements of the Federal Prison Industries, Inc. (FPI), a bureau of the United States Department of Justice (DOJ), as of and for the year ended September 30, 2000 and have issued our qualified report thereon, dated January 5, 2001. 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. 01-02, *Audit Requirements for Federal Financial Statements*.

In planning and performing our audit, we considered FPI's internal control over financial reporting by obtaining an understanding of FPI's internal control, determined whether internal controls had been placed in operation, assessed control risk, and performed tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin No. 01-02. We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982 (FMFIA), such as those controls relevant to ensuring efficient operations. The objective of our audit was not to provide assurance on internal control. Consequently, we do not provide an opinion on internal control.

Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control that, in our judgment, could adversely affect FPI's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

*Independent Auditor's Report on Internal Control, continued*

Because of inherent limitations in internal controls, misstatements, losses, or noncompliance may nevertheless occur and not be detected. However, we noted certain matters involving the internal control and its operation that we consider to be reportable conditions, and, with respect to the first five below, material weaknesses.

The conditions detailed on the following pages are summarized as follows:

1. FPI does not have adequate controls over inventories. (New finding)
2. FPI does not have adequate controls over accounts receivable. (New finding)
3. FPI does not have adequate controls over cash reconciliation procedures and cash transaction processing. (New finding)
4. FPI needs improvement in the financial statement preparation process. (New finding)
5. FPI information security program management and controls require improvement. (New finding)
6. FPI does not have adequate controls over accounting and reporting of leases and the procurement of property, plant and equipment. (New finding)

We also noted other matters involving the internal control and its operation, which we have reported to the management of FPI in a separate letter, dated January 5, 2001.

This report is intended solely for the information and use of the Office of the Inspector General, the management of FPI and the Department of Justice, the FPI Board of Directors, OMB and Congress, and is not intended to be and should not be used by anyone other than these specified parties.



Washington, DC  
January 5, 2001

*Detailed information concerning the reportable conditions noted in Federal Prison Industries, Inc. internal control report can be obtained from the Department of Justice, Office of Inspector General for Audit, Office of Policy and Planning, 1425 New York Avenue, NW, Suite 5000, Washington, DC 20530 and from the Internet site at [www.unicor.gov](http://www.unicor.gov).*

***Independent Auditor's Report on Compliance with Laws and Regulations***

Office of the Inspector General  
United States Department of Justice

Board of Directors  
Federal Prison Industries, Inc.

We have audited the financial statements of the Federal Prison Industries, Inc. (FPI), a bureau of the United States Department of Justice, as of and for the year ended September 30, 2000, and have issued our qualified report thereon dated January 5, 2001. 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. 01-02, *Audit Requirements for Federal Financial Statements*.

The management of FPI is responsible for complying with laws and regulations applicable to the agency. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of FPI's compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain other laws and regulations specified in OMB Bulletin No. 01-02, including the requirements referred to in the Federal Financial Management Improvement Act (FFMIA) of 1996. We limited our tests of compliance to these provisions and we did not test compliance with all laws and regulations applicable to Federal Prison Industries, Inc.

The results of our tests of compliance with the laws and regulations described in the preceding paragraph, exclusive of FFMIA, disclosed instances of noncompliance with the following laws and regulations that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 01-02. Specifically, FPI is not in compliance with provisions of the Prompt Payment Act as described below:

FPI's accounting system of record, SAP, is unable to calculate and accrue interest on unpaid obligations to suppliers and vendors that exceed statutorily defined prompt payment periods. Accordingly, FPI manually performs calculations to accrue interest on these unpaid obligations. However, as of September 30, 2000, FPI had not paid any of the accrued amounts owed.

Under FFMIA, we are required to report whether FPI's financial management systems substantially comply with the Federal financial management systems requirements, applicable Federal accounting standards, and the United States Government Standard General Ledger at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA section 803 (a) requirements.

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*Independent Auditor's Report on Compliance with Laws and Regulations, continued*

The results of our tests disclosed instances where FPI's financial management systems did not substantially comply with Federal financial management systems requirements as described below:

FPI's financial management systems do not meet specific Federal financial management system requirements, defined within OMB Circular A-130, *Management of Federal Information Resources*.

Specific conditions attributable to this noncompliance are more fully described in our report on internal control dated January 5, 2001. FPI's Management Information Systems Branch is responsible for the financial management systems within FPI.

Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion.

This report is intended solely for the information and use of the Office of the Inspector General, the management of FPI and the Department of Justice, the FPI Board of Directors, OMB and Congress, and is not intended to be and should not be used by anyone other than these specified parties.



Washington, DC  
January 5, 2001

Federal Prison Industries, Inc.  
**Statements of Financial Position**

**September 30**

(DOLLARS IN THOUSANDS)

	2000	1999
<b>Asset</b>		
Current:		
Cash and cash equivalents	\$ 37,354	\$ 89,309
Accounts receivable, net	103,279	86,123
Inventories, net	118,074	92,373
Other assets	3,298	434
	262,005	268,239
Property, plant and equipment, net	141,620	146,621
<b>Total Assets</b>	<b>\$403,625</b>	<b>\$414,860</b>

**Liabilities and United States Government Equity**

Current:

Accounts payable	\$ 60,306	\$ 41,801
Deferred revenue	21,842	31,312
Accrued salaries and wages	10,829	15,160
Accrued annual leave	7,387	6,785
Accrued expenses	8,396	12,900
	108,760	107,958
Note payable to United States Treasury	20,000	20,000
<b>Total liabilities</b>	<b>128,760</b>	<b>127,958</b>

United States Government Equity

Initial capital	4,176	4,176
Donated property	135	384
Cumulative results of operations	270,554	282,342
<b>Total United States Government Equity</b>	<b>274,865</b>	<b>286,902</b>
<b>Total Liabilities and United States Government Equity</b>	<b>\$ 403,625</b>	<b>\$ 414,860</b>

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

Federal Prison Industries, Inc.

**Statements of Operations and Cumulative Results of Operations*****Fiscal years ended September 30****(DOLLARS IN THOUSANDS)*

	<b>2000</b>	<b>1999</b>
Net sales	\$ 546,347	\$ 566,172
Cost of sales	512,021	505,111
Gross profit	34,326	61,061
Interest and other income	21,321	12,795
Selling, general and administrative expenses	(67,435)	(57,239)
Net income (loss)	(11,788)	16,617
Cumulative results of operations, beginning of fiscal year	282,342	265,725
Cumulative results of operations, end of fiscal year	\$ 270,554	\$ 282,342

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

Federal Prison Industries, Inc.  
**Statements of Cash Flows**

**Fiscal years ended September 30**

<i>(DOLLARS IN THOUSANDS)</i>	<b>2000</b>	<b>1999</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Cash received—customers	\$ 529,191	\$ 585,627
Cash received—interest	3,108	2,540
Cash paid—suppliers and other vendors	(410,683)	(423,361)
Cash paid—civilian and inmate payrolls	(165,782)	(150,237)
Net cash provided by (used in) operating activities	(44,166)	14,569
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Net purchases of property, plant and equipment	(6,954)	(5,671)
Construction-in-progress of plant facilities	(835)	(1,317)
Net cash used in investing activities	(7,789)	(6,988)
Net increase (decrease) in cash and cash equivalents	(51,955)	7,581
Cash and cash equivalents, beginning of fiscal year	89,309	81,728
Cash and cash equivalents, end of fiscal year	\$ 37,354	\$ 89,309
<b>RECONCILIATION OF NET INCOME (LOSS) TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES</b>		
Net income (loss)	\$ (11,788)	\$ 16,617
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	12,511	10,845
Loss on disposal of property, plant and equipment	30	37
Changes in:		
Accounts receivable	(17,156)	(17,666)
Inventories	(25,701)	(2,426)
Other assets	(2,864)	693
Accounts payable	18,505	5,373
Deferred revenue	(9,470)	(8,495)
Accrued salaries and wages	(4,331)	6,482
Accrued annual leave	602	504
Accrued expenses	(4,504)	2,605
Net cash provided by (used in) operating activities	\$ (44,166)	\$ 14,569

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

Federal Prison Industries, Inc.  
**Fiscal Year 2000**  
**Notes to Financial Statements**

**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 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 agencies such as the Department of Justice, the Department of Defense, the Postal Service, the Veterans Administration, and the General Services Administration. These and other federal organizations are required to purchase products from FPI, if its products meet the customers' price, quality, and delivery standards, under a mandatory source preference specified in FPI's enabling statute and the Federal Acquisition Regulation.

As of September 30, 2000, FPI had industrial operations at 103 factories located at 68 facilities within the Federal Prison System; these factories employed approximately 21,700 inmates representing approximately 18% of the total federal inmate population.

**NOTE 2**

**SUMMARY OF  
SIGNIFICANT  
ACCOUNTING  
POLICIES**

***Basis of Presentation***

FPI has historically prepared its external financial statements in conformity with 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 generally accepted accounting principles. FASAB has indicated, however, that accounting standards published by FASB may also be in accordance with generally accepted accounting principles for those federal entities, including FPI, that have issued such financial statements in the past.

These financial statements consolidate all of FPI's industrial facilities located throughout the Federal Prison System and its central administrative offices located in Washington, D.C. All interfacility and interfactory transactions have been eliminated for financial reporting purposes.

***Use of Estimates***

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could 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 cash equivalents are comprised of short-term overnight repurchase agreements with the United States Department of Treasury. The market value of these repurchase agreements is equivalent to cost. Certain portions of FPI's cash balance have

Federal Prison Industries, Inc.  
**Notes to Financial Statements**

been internally restricted to provide for future debt repayment (Note 7) and to fund future purchases of inventory.

**Accounts Receivable**

Accounts receivable are stated net of an allowance for doubtful accounts. Billed accounts receivable consist of amounts due from federal government agencies and departments as well as certain private sector entities. In accordance with generally accepted contract accounting methods, unbilled receivables may result from revenue that has been earned but not yet billed until contractually defined intervals or milestones have been achieved. FPI routinely assesses the collectibility of its accounts receivable and maintains allowances for anticipated losses.

**Inventories**

Inventories are stated at the lower of cost or market with cost determined on a weighted-average method under the first in, first out basis. Recorded amounts are periodically adjusted to reflect the results of physical inventory counts. FPI has established inventory valuation and obsolescence allowances in anticipation of losses on contracts in which the total manufacturing cost exceeds the total sales price, and also for inventories that may not be utilized in future periods.

**Other Assets**

Other assets include advances to suppliers, other receivables and prepayments.

**Revenue Recognition**

Revenue is generally recognized upon shipment of goods to customers and upon performance of services. FPI sells a wide range of products to a diversified base of customers, primarily governmental agencies and departments.

Revenue from long-term or fixed price contracts is recognized using generally accepted contract accounting methods. Revenue from contracts that specify a customer acceptance criteria is not recognized until either customer acceptance is obtained or upon completion of the contract. Provisions for anticipated contract losses are recognized at the time that they become evident.

Cost of sales is comprised primarily of inventory cost, labor costs for services performed and provisions for contract losses.

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.

**Property, Plant and Equipment**

Property, plant and equipment are stated at cost, net of an allowance for accumulated depreciation. Donated property and equipment, which is recorded at appraisal value at the date of donation, principally relates to property and equipment transferred from other government agencies and departments. Depreciation is computed using the straight line method over the estimated useful lives of the assets, which generally range between 5 and 40 years. Upon retirement or disposition of property and equipment, the related gain or loss is reflected in the statement 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.

Federal Prison Industries, Inc.  
**Notes to Financial Statements**

**Reclassifications**

Certain fiscal year 1999 financial statement line items have been reclassified to conform with the current year's presentation.

**NOTE 3**

Accounts receivable, net consists of the following:

**September 30**

(DOLLARS IN THOUSANDS)

	<b>2000</b>	<b>1999</b>
Intra governmental billed receivables	\$103,938	\$83,012
Intra governmental unbilled receivables	-	4,157
Non-governmental billed receivables	6,011	1,277
	109,949	88,446
Less allowance for doubtful accounts	6,670	2,323
<b>Accounts receivable, net</b>	<b>\$103,279</b>	<b>\$86,123</b>

**NOTE 4**

Inventories, net consist of the following:

**September 30**

(DOLLARS IN THOUSANDS)

	<b>2000</b>	<b>1999</b>
Raw materials	\$ 65,984	\$ 47,055
Work-in-process	19,834	23,869
Finished sub-assemblies	11,737	4,650
Finished goods	39,302	23,480
	136,857	99,054
Less inventory allowance	18,783	6,681
<b>Inventories, net</b>	<b>\$118,074</b>	<b>\$ 92,373</b>

Federal Prison Industries, Inc.  
**Notes to Financial Statements**

**NOTE 5**

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

<b>PROPERTY, PLANT AND EQUIPMENT, NET</b>	<b>September 30</b>	
	<i>(DOLLARS IN THOUSANDS)</i>	
	<b>2000</b>	<b>1999</b>
Machinery, equipment, and software	\$ 97,615	\$ 95,471
Buildings and improvements	165,959	164,800
	263,574	260,271
Less accumulated depreciation	122,789	114,967
	140,785	145,304
Factory construction-in-progress	835	1,317
<b>Property, plant and equipment, net</b>	<b>\$141,620</b>	<b>\$146,621</b>

Depreciation and amortization expense approximated \$12,511,000 and \$10,845,000 for the years ended September 30, 2000 and 1999, respectively.

**NOTE 6**

Accrued expenses consist of the following:

<b>ACCRUED EXPENSES</b>	<b>September 30</b>	
	<i>(DOLLARS IN THOUSANDS)</i>	
	<b>2000</b>	<b>1999</b>
Permanent change of station	\$ 3,033	\$ 2,028
Information systems	2,994	1,075
FECA liability	1,188	613
Other expense	1,181	9,184
<b>Accrued expenses</b>	<b>\$ 8,396</b>	<b>\$ 12,900</b>

**NOTE 7****NOTE PAYABLE  
TO UNITED  
STATES  
TREASURY**

Congress has granted FPI borrowing authority pursuant to Public Law 100-690. Under this authority, FPI has borrowed \$20,000,000 from the United States Treasury ("the Treasury") with an extended lump-sum maturity date of September 30, 2008. The funds received under this note have been internally restricted for use in the construction of plant facilities and the purchase of equipment. The note accrues interest, payable March 31 and September 30 of each fiscal year at 5.5% (the rate equivalent to the yield of United States Treasury obligations of comparable maturities which existed on the date of a note maturity extension, granted in fiscal year 1998). Accrued interest payable under the note is either fully or partially offset to the extent FPI maintains non-interest bearing cash deposits with the Treasury. In this regard,

Federal Prison Industries, Inc.  
**Notes to Financial Statements**

there is no accrual of interest unless FPI's daily cash balance on deposit with the Treasury is less than the unpaid principal balance of all note advances received, as determined by a monthly calculation performed by the Treasury. When FPI's daily cash balance is less than the unpaid principal balance of all note advances received, interest is calculated by the Treasury on the difference between these two amounts. The note agreement provides for certain restrictive covenants and a prepayment penalty for debt retirements prior to 2008. Additionally, the agreement limits authorized borrowing in an aggregate amount not to exceed 25% of FPI's net equity.

There was no interest expense for the years ended September 30, 2000 and 1999.

**NOTE 8**

FPI's revenue generating operations consist of five principal product programs. Net sales consist of the following:

**PRODUCT SALES  
INFORMATION****Net Sales****Fiscal years ended September 30***(DOLLARS IN THOUSANDS)*

	2000	1999
<i>Product Programs</i>		
Metals/Systems	\$109,139	\$124,396
Furniture	118,995	128,461
Electronics/Plastics	133,930	129,428
Graphics/Services	51,757	47,871
Clothing/Textiles	132,526	136,016
<b>Net sales</b>	<b>\$546,347</b>	<b>\$566,172</b>

**NOTE 9**

FPI's financial activities interact with and are dependent upon those of the federal government as a whole. The following is a discussion of certain inter/intra-governmental activities and their related interaction with FPI:

**INTER/INTRA-  
GOVERNMENTAL  
FINANCIAL  
ACTIVITIES****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 respective missions requires the sharing of facilities and responsibilities relative to the custody, training and employment of federal inmates. The Director of the BOP serves as the Chief Executive Officer of FPI and the Chief Operating Officer of FPI 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.

**Self Insurance**

In accordance with federal government policy, FPI is uninsured with respect to property

Federal Prison Industries, Inc.  
**Notes to Financial Statements**

damage, product liability, and other customary business loss exposures. Losses incurred are absorbed as a current operating expense 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 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. During the fiscal years ended September 30, 2000 and 1999, such claims and benefits, as charged to FPI, approximated \$1,209,000 and \$613,000, 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, which is included with other accrued expenses, approximated \$5,710,000 and \$4,501,000 at September 30, 2000 and 1999, respectively.

***Retirement***

Substantially all of FPI's civilian employees are covered under either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). For employees covered under CSRS (those employees hired prior to January 1, 1984), FPI withholds approximately 7 percent (for normal retirement) or 7.5 percent (for hazardous duty retirement) of each employee's salary and contributes a matching amount to the fund. CSRS covered employees do not have Federal Insurance Contributions Act (FICA) withholdings and, thus, are not fully eligible to receive Social Security benefits. For employees covered under FERS (generally those employees hired on or after January 1, 1984), FPI withholds, in addition to FICA withholdings, approximately 1.3 percent of employee gross earnings, and matches such withholdings with a 7.0 percent contribution.

Under FERS, 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) up to 10 percent of salary to an investment fund. FPI then matches this amount up to 5 percent. Those employees which elected to remain under CSRS after January 1, 1984 continue to receive benefits in place, and may also contribute (tax deferred) up to 5 percent of their salary to the thrift plan, but with no matching amount contributed by FPI.

CSRS and FERS 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 U.S. Office of Personnel Management.

FPI's contribution to both plans was approximately \$16,615,000 and \$15,297,000 for the years ended September 30, 2000 and 1999, respectively.

Federal Prison Industries, Inc.  
**Notes to Financial Statements**

In addition, under Statement of Federal Financial Accounting Standards No. 5, *Accounting for Liabilities of the Federal Government (SFFAS No. 5)*, FPI is required to recognize its share of the true cost of providing pension benefits to eligible employees utilizing cost factors determined by the Office of Personnel Management. SFFAS No. 5 had the effect of increasing pension expense, a component of selling and administrative expense by approximately \$3,349,000 and \$3,814,000 in the fiscal years ended September 30, 2000 and 1999, respectively, with an offsetting credit to other income in each respective year. However, because of the offsetting credit, as more fully disclosed in Note 10 to the financial statements, the recording of these costs have no impact on reported net income(loss).

***Health Benefits and Life Insurance***

FPI, through the Office of Personnel Management (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 approximated \$4,023,000 and \$5,241,000 for the years ended September 30, 2000 and 1999, respectively.

OPM also provides health care and life insurance benefits for FPI's retired employees. Under SFFAS No. 5, FPI is also required to recognize as an expense 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 \$4,038,000 and \$3,985,000 during the fiscal years ended September 30, 2000 and 1999, respectively, were determined by OPM utilizing cost factors which estimate the cost of providing post retirement benefits to current employees. However, because of the offsetting credit, as fully disclosed in Note 10 to the financial statements, the recording of these costs have no impact on reported net income(loss).

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 by OPM.

Federal Prison Industries, Inc.  
**Notes to Financial Statements**

**NOTE 10**

Selling, general and administrative expenses consist of the following:

**SELLING,  
GENERAL AND  
ADMINISTRATIVE  
EXPENSES**

***Selling, general and administrative expenses***

***Fiscal years ended September 30***

<i>(DOLLARS IN THOUSANDS)</i>	<b>2000</b>	<b>1999</b>
Salaries, wages and benefits	\$ 34,852	\$ 30,840
Permanent change of station expense	3,095	2,244
Purchases of minor equipment	3,679	1,000
Contract services	5,596	2,592
Bad debt expense	6,259	2,375
Credit card services	1,294	1,577
Travel	2,776	1,780
Other Expense	9,884	14,831
Imputed pension costs (Note 9)	3,349	3,814
Imputed post-retirement health care and life insurance cost (Note 9)	4,038	3,985
SFFAS No. 5 offsetting credit relating to expense recognition of imputed financing costs (Note 9)	(7,387)	(7,799)
	<b>\$ 67,435</b>	<b>\$ 57,239</b>

**NOTE 11**

**COMMITMENTS  
AND  
CONTINGENCIES**

***Legal Contingencies***

FPI is a defendant in a litigation matter in which plaintiffs allege, among other things, that FPI improperly expanded production of its office seating, office case goods, and systems furniture beginning in 1989. The plaintiffs request declaratory and injunctive relief, including the return of competitive market sales of at least \$450 million. FPI maintains its practices have been lawful and that plaintiffs are not entitled to the relief requested. Discovery is ongoing.

Various other litigation matters exist that involve contract law, employment law, and constitutional law issues. FPI does not believe these case matters are significant in nature, nor that an unfavorable outcome would adversely affect FPI or its continuing operations.

***Lease Commitments***

FPI leases certain facilities, machinery, vehicles and office equipment under noncancellable operating lease agreements that expire over future periods. Many of these 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. Future commitments under these

Federal Prison Industries, Inc.  
**Notes to Financial Statements**

agreements are not significant. Rental expense for the fiscal years ended September 30, 2000 and 1999 was approximately \$2,540,000 and \$674,000, respectively.

***Planned Construction***

As of September 30, 2000, various projects were in progress for the construction of new industrial facilities and the renovation of existing facilities. In this regard, BOP, on behalf of FPI, is planning to invest approximately \$10.2 million during the next fiscal year for the construction of buildings and improvements. In addition, during the next fiscal year, FPI is planning to invest approximately \$3.9 million for the purchase of machinery and equipment.

***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:

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***Congressional limitation on administrative expenses***

***Fiscal years ended September 30***

<i>(DOLLARS IN THOUSANDS)</i>	<b>2000</b>	<b>1999</b>
Congressional limitation on expenses	\$3,429	\$3,266
Expenses incurred subject to Congressional limitation	\$1,634	\$1,272

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