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Independent Auditors' Report on Compliance and Other Matters

United States Attorney General
U. S. Department of Justice

Inspector General
U. S. Department of Justice

We have audited the consolidated balance sheets of the U.S. Department of Justice (the Department) as of September 30, 2006 and 2005, and the related consolidated statements of net cost, changes in net position, and financing, and combined statements of budgetary resources and custodial activity (hereinafter referred to as "consolidated financial statements") for the years then ended, and have issued our report thereon dated November 10, 2006. That report indicated that we did not audit the financial statements of the following components of the Department: the U.S. Marshals Service (USMS); the Federal Bureau of Prisons (BOP); and the Federal Prison Industries, Inc. (FPI). Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our report, insofar as it related to the amounts included for those components, was based solely on the reports of the other auditors. As discussed in Note 18 to the consolidated financial statements, the Department changed its method of reporting earmarked funds to adopt the provisions of the Federal Accounting Standards Advisory Board's Statement of Federal Financial Accounting Standards No. 27, *Identifying and Reporting Earmarked Funds*, effective October 1, 2005.

We and the other auditors 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 (OMB) Bulletin No. 06-03, *Audit Requirements for Federal Financial Statements*. Those standards and OMB Bulletin No. 06-03 require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement.

As noted above, we did not audit the financial statements of the USMS, BOP, and FPI. Those financial statements were audited by other auditors whose reports thereon, including the other auditors' *Independent Auditors' Reports on Compliance and Other Matters*, have been furnished to us. Our report on the Department's compliance and other matters, insofar as it relates to these components, is based solely on the reports and findings of the other auditors.

The management of the Department is responsible for complying with laws, regulations, contracts, and grant agreements applicable to the Department. As part of obtaining reasonable assurance about whether the Department's fiscal year 2006 consolidated financial statements are free of material misstatement, we and the other auditors performed tests of the Department's compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of the consolidated financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 06-03, including certain requirements referred to in the *Federal Financial Management Improvement Act of 1996* (FFMIA). We and the other auditors limited our tests of compliance to the provisions described in the preceding sentence, and we did not test compliance with all



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laws, regulations, contracts, and grant agreements applicable to the Department. 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 and the other auditors' tests of compliance described in the preceding paragraph of this report, exclusive of those referred to in FFMIA, disclosed the following instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 06-03:

- *Prompt Payment Act* – The USMS did not always include payment of interest on late payments, nor did it always notify the vendors within seven days of receipt in instances where bills were in dispute.
- OMB Circular No. A-11, *Preparation, Submission, and Execution of the Budget* – In fiscal year 1993, the USMS entered into a capital lease without reserving sufficient budget authority to meet the scorekeeping requirements of the OMB circular.

Under OMB Bulletin No. 06-03 and FFMIA, we are required to report whether the Department's financial management systems substantially comply with: (1) Federal financial management systems requirements, (2) applicable Federal accounting standards, and (3) 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.

The results of our and the other auditors' tests disclosed instances, described below, in which the components did not substantially comply with the three requirements discussed in the preceding paragraph:

- Federal Financial Management System Requirements – The Office of Justice Programs (OJP); Federal Bureau of Investigation (FBI); Bureau of Alcohol, Tobacco, Firearms and Explosives (ATF); and USMS financial management systems do not meet Federal financial management systems requirements, in that deficiencies were noted in entity-wide security, access and change controls, service continuity, interface controls, system software, and segregation of duties.
- Federal Accounting Standards – Certain component entities (FBI, ATF, and USMS) do not initially record financial transactions in accordance with Statements of Federal Financial Accounting Standards (SFFAS). Specifically, deficiencies were reported in the following areas:
 - FBI – Managerial cost accounting
 - ATF – Accounts payable
 - USMS – Intra-fund transactions, accrued payroll and accounts payable, construction work-in-progress, budgetary reimbursable transactions, and reconciliation of budgetary and proprietary data in the Statement of Financing
- United States Standard General Ledger (USSGL) at the Transaction Level – Certain component entities (FBI and USMS) do not record all entries in their financial management systems at the USSGL transaction level. Specifically, deficiencies were reported in the following areas:
 - FBI – certain transactions are processed outside of the core financial accounting system, but they are not recorded at the transaction level using the USSGL. These transactions must be modified when recorded into the core financial accounting system through a manual or automated batch transaction process.



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- USMS – transaction detail for upward and downward adjustments of prior-year undelivered orders is not maintained and capitalized property adjustments and budgetary reimbursable activity is not recorded in accordance with USSGL posting logic.

All significant facts pertaining to the matters referred to above, including the required elements of the findings and the recommended remedial actions, are included in the components' auditors' *Independent Auditors' Reports on Internal Control* or *Independent Auditors' Reports on Compliance and Other Matters*.

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

KPMG LLP

November 10, 2006

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