
OFFICE OF THE INSPECTOR GENERAL COMMENTARY AND SUMMARY

This audit report contains the Annual Financial Statement of the U.S. Department of Justice (Department) for the fiscal year ended September 30, 2003. Under the direction of the Office of the Inspector General (OIG), PricewaterhouseCoopers LLP performed the consolidated Department audit and five of the eleven component audits. Two other independent public accounting firms performed the remaining six component audits, upon which PricewaterhouseCoopers LLP relied when issuing the report on the consolidated financial statements.

The Department received an unqualified opinion on its FY 2003 financial statements. This is the third straight year the Department received an unqualified opinion on its consolidated financial statements, and the Department deserves credit for this accomplishment.

However, the clean opinion on the consolidated audit came at tremendous cost and effort because the Department lacks sufficient automated systems to readily support ongoing accounting operations and financial statement preparation. Many tasks were performed manually at the end of the year rather than being performed throughout the fiscal year. Most components' management systems are not integrated with their financial accounting systems, requiring manual reconciliations between the two systems to support amounts reported on the financial statements. These significant, costly, and time-intensive manual efforts will continue to be necessary for the Department and its components to produce financial statements until automated, integrated processes and systems are implemented that readily produce the necessary information throughout the year.

While some Department components struggled to successfully complete their audits and required extensive substantive testing of account balances at year-end, others readily met the Department's expedited timelines. The key to success was the quality of accounting records throughout the year. If the Department is to succeed in further expediting its reporting, there cannot be massive clean-up efforts at year end. Rather, there must be effective controls in place that are enforced and monitored throughout the year to ensure accurate, timely financial information is continually available. This will require changes in financial management processes and full participation of all involved, including program, budget, and administrative offices. We are concerned that without these fundamental changes the Department will not be able to meet the Office of Management and Budget's (OMB) accelerated reporting date of November 15 for FY 2004 and subsequent years. In order to meet the OMB due date, the Department will have to complete its Performance & Accountability Report 2½ months earlier than it did in FY 2003.

The Department's FY 2003 consolidated report on internal control included two repeat reportable conditions, one of which is considered a material weakness. This represents an improvement in the number of consolidated material weaknesses, as the Department was able to reduce to a reportable condition one of the two material weaknesses reported for FY 2002 (weaknesses with components' financial systems general and application controls). However, the remaining material weakness on financial controls was much more serious than in past years and as a result the auditors noted in their report the decline in financial controls.

The Department's components had mixed results, with some able to successfully address previously reported conditions, while others had new conditions identified and reported this year. Although the auditors reported a total of nine material weaknesses and ten reportable conditions for both FY 2003 and 2002 for the components, the mix among the components differed from last year. The table on page 152 compares the FY 2003 and the FY 2002 audit results for the Department consolidated audit as well as for the eleven individual component audits. The consolidated report on internal control includes both the Bureau of Alcohol, Tobacco, Firearms and Explosives (ATF) and the Immigration and Naturalization Service (INS). The INS was transferred to the Department of Homeland Security on March 1, 2003, and ATF was transferred into the Department of Justice on January 24, 2003, from the Department of the Treasury, pursuant to the Homeland Security Act of 2002, Public Law 107-296. The Department of Homeland Security will be responsible for follow-up on INS issues.

The Department's financial material weakness was more serious this year because of the overall decline in the effectiveness of the controls identified in financial accounting and reporting. Issues were identified at eight of the eleven Department components. The weaknesses include (1) financial management systems not integrated or not configured to support financial management and reporting; (2) not recording financial transactions (assets, liabilities, revenue, property, and inventories in particular) in accordance with generally accepted accounting principles; and (3) not having effective financial statement preparation processes to ensure financial statements were completed timely and in conformance with the Department's requirements. Additional issues relating to the preparation of the Department's consolidated financial statements and with reconciling intra-departmental and intra-governmental transactions were also noted.

In the FY 2003 consolidated report on compliance with laws and regulations, the auditors identified six Department components that were not compliant with the Federal Financial Management Improvement Act of 1996 (FFMIA), which requires compliance with Federal financial management systems requirements, applicable Federal accounting standards, and the United States standard general ledger at the transaction level. The six non-compliant components were the Federal Bureau of Investigation (FBI); the INS; the Offices, Boards and Divisions (OBD); the Working Capital Fund (WCF); the Assets Forfeiture Fund and Seized Asset Deposit Fund; and the United States Marshals Service (USMS). The FBI, INS, OBD, and WCF were also not compliant with FFMIA in FY 2002. Additionally, the auditors identified five Department components that were not compliant with OMB Circular No. A-11, *Preparation, Submission and Execution of the Budget*, which among other items requires (1) that agencies fund the net present value of the Government's estimated legal obligation over the life of a leased asset and (2) that an unfilled customer order (for services performed) or an obligation (for services acquired) be recorded at the time an agreement/contract to commit the Federal government is signed. The FBI, ATF, and USMS do not fully fund the acquisition of leased assets at the inception of the lease, and the OBD and WCF do not record the full amount of an unfilled customer order (for services performed) or an obligation (for services acquired), when a reimbursable agreement or contract to provide/acquire goods or services is signed.

The Department not only faces the challenge of accelerated due dates for FY 2004, but the selection and implementation of a Department-wide unified financial system. To continue improving financial management, the Department must concentrate on standardizing and integrating financial processes and systems to more efficiently support accounting operations, preparation of financial statements, and audit processes. Additionally the Department must be willing to dedicate the appropriate staff and resources to these efforts.

The OIG reviewed PricewaterhouseCoopers LLP's report and related documentation and made necessary inquiries of its representatives. Our review, as differentiated from an audit in accordance with U.S. generally accepted government auditing standards, was not intended to enable us to express, and we do not express, an opinion on the Department's financial statements, conclusions about the effectiveness of internal control, or conclusions on compliance with laws and regulations. PricewaterhouseCoopers LLP is responsible for the attached auditor's report dated January 16, 2004, and the conclusions expressed in the report. However, our review, while still ongoing, disclosed no instances where PricewaterhouseCoopers LLP did not comply, in all material respects, with generally accepted government auditing standards.

Comparison of FY 2003 and FY 2002 Audit Results						
Reporting Entity	Auditors' Opinion On Financial Statements		Number of Material Weaknesses¹		Number of Reportable Conditions²	
	2003	2002	2003	2002	2003	2002
Consolidated Department of Justice	Unqualified ³	Unqualified	1	2	1	0
Offices, Boards and Divisions	Unqualified	Unqualified	1	1	1	1
Assets Forfeiture Fund and Seized Asset Deposit Fund	Unqualified	Unqualified	1	0	0	1
Federal Bureau of Investigation	Unqualified	Unqualified	2	3	0	0
Drug Enforcement Administration	Unqualified	Unqualified	0	0	2	2
Office of Justice Programs	Unqualified	Unqualified	0	0	1	1
Immigration and Naturalization Service ⁴	Unqualified	Unqualified	3	3	1	0
U.S. Marshals Service	Unqualified	Unqualified	1	0	1	2
Federal Bureau of Prisons	Unqualified	Unqualified	0	0	2	2
Federal Prison Industries, Inc.	Unqualified	Unqualified	0	1	1	1
Working Capital Fund	Unqualified	Unqualified	1	1	0	0
Bureau of Alcohol, Tobacco, Firearms and Explosives ⁴	Unqualified	N/A	0	N/A	1	N/A
Component Totals			9	9	10	10

¹ A material weakness is a reportable condition (see below) in which the design or operation of the internal control does not reduce to a relatively low level the risk that error, fraud, or noncompliance in amounts that would be material in relation to the principal statements or to performance measures may occur and not be detected within a timely period by employees in the normal course of their assigned duties.

² A reportable condition includes matters coming to the auditor's attention that, in the auditor's judgment, should be communicated because they represent significant deficiencies in the design or operation of internal controls that could adversely affect the entity's ability to properly report financial data.

³ Unqualified opinion -- An auditor's report that states the financial statements present fairly, in all material respects, the financial position and results of operations of the reporting entity, in conformity with generally accepted accounting principles.

⁴ Pursuant to the Homeland Security Act of 2002, Public Law 107-296, the Immigration and Naturalization Service transferred to the Department of Homeland Security on March 1, 2003. Additionally, the Bureau of Alcohol, Tobacco, Firearms and Explosives transferred from the Department of the Treasury into the Department of Justice on January 24, 2003.