U. S. DEPARTMENT OF JUSTICE
ANNUAL FINANCIAL STATEMENT
FISCAL YEAR 2007

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 (FY) ended September 30, 2007. Under the direction of the Office of the Inspector General (OIG), KPMG LLP performed the consolidated Department audit and eight of the nine component audits. Another independent public accounting firm, Cotton & Company, LLP, performed the remaining component audit, upon which KPMG LLP relied when issuing its report on the consolidated financial statements. For FY 2006, KPMG LLP also performed the consolidated Department audit, and 7 of the 10 component audits. Beginning in FY 2007 the activities and balances of the Department's Working Capital Fund, previously reported separately, are included in the Offices, Boards and Divisions consolidated and combined financial statements.

The Department received an unqualified opinion on its FYs 2007 and 2006 financial statements. This year, at the consolidated level the Department had two significant deficiencies, compared to one material weakness and one reportable condition for FY 2006. Effective for FY 2007, the term "reportable condition" was changed to the term "significant deficiency," and new definitions of material weakness and significant deficiency were introduced in auditing standards generally accepted in the United States. See *Government Auditing Standards* and Office of Management Budget Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*.

Both of the Department's significant deficiencies are repeat issues, which were reported as one material weakness and one reportable condition during FY 2006. For FY 2007, weaknesses in the general and application controls for each of the Department's component financial systems were reported as a significant deficiency, with the exception of the Federal Bureau of Investigation (FBI) where it was classified as a material weakness. The Department's significant deficiency related to financial reporting includes several serious but isolated issues, including the U.S. Marshals Service's (USMS) financial accounting and reporting quality-control and assurance, and funds management controls; the Bureau of Alcohol, Tobacco, Firearms and Explosives' (ATF) accounts payable process; the Office of Justice Programs' (OJP) grant advance and payable estimation process, and grant deobligation process; the Offices, Boards and Divisions' (OBDs) status of obligations controls, and preparation, review, and approval of journal entries; and the Assets Forfeiture Fund and Seized Asset Deposit Fund's (AFF/SADF) obligations and disbursements controls, and seized and forfeited property controls.

While the Department's financial statement audit results have continued to improve, the Department still lacks sufficient automated systems to readily support ongoing accounting operations and financial statement preparation. Inadequate, outdated, and in some cases non-integrated financial management systems do not provide certain automated financial transaction processing activities that are necessary to support management's need for timely and accurate financial information throughout the year. Many tasks still must be performed manually at interim periods and at year end, requiring extensive manual efforts on the part of financial and audit personnel. 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 the Department is proceeding towards a Unified Financial Management System (UFMS) that it believes will correct many of these issues, implementation has been slow and will not be completed across the Department for at least another 5 years.

In the FY 2007 consolidated report on compliance and other matters, the auditors identified no instances of significant non-compliance with applicable laws and regulations. Although some instances of non-compliance were reported at some of the components, the consolidated auditors determined that none of the component level non-compliance issues caused the Department as a whole to be in significant non-compliance.

The OIG reviewed KPMG LLP's reports and related documentation and made necessary inquiries of its representatives. Our review, as differentiated from an audit in accordance with United States 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. KPMG LLP is responsible for the attached auditors' reports dated November 9, 2007, and the conclusions expressed in the reports. However, our review, while still ongoing, disclosed no instances where KPMG LLP did not comply, in all material respects, with generally accepted government auditing standards.

Comparison of FY 2007 and FY 2006 Audit Results

Reporting Entity	Auditors' Opinion On Financial Statements		Number of Material Weaknesses[1]				Number of Significant Deficiencies[2]			
			Financial		Information Systems		Financial		Information Systems	
	2007	2006	2007	2006	2007	2006	2007	2006	2007	2006
Consolidated DOJ	U[3]	U	0	0	0	1	1	1	1	0
OBDs	U	U	0	0	0	0	2	0	1	1
AFF/SADF	U	U	0	0	0	0	2	1	1	1
FBI	U	U	0	0	1	1	0	0	0	0
DEA	U	U	0	0	0	0	0	0	1	0
OJP	U	U	0	1	0	1	2	1	1	0
USMS	U	U	2	1	0	1	0	0	1	0
BOP	U	U	0	0	0	0	0	0	1	1
FPI	U	U	0	0	0	0	0	0	1	0
WCF[4]	N/A	U	N/A	0	N/A	0	N/A	1	N/A	1
ATF	U	U	1	1	0	1	0	0	1	0
Component Totals			3	3	1	4	6	3	8	4

Consolidated Department of Justice (Consolidated DOJ); Offices, Boards and Divisions (OBDs); Assets Forfeiture Fund and Seized Asset Deposit Fund (AFF/SADF); Federal Bureau of Investigation (FBI); Drug Enforcement Administration (DEA); Office of Justice Programs (OJP); U.S. Marshals Service (USMS); Federal Bureau of Prisons (BOP); Federal Prisons Industries (FPI); Working Capital Fund (WCF); Bureau of Alcohol, Tobacco, Firearms and Explosives (ATF)

[1] A material weakness is a significant deficiency (see below), or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Department's internal control.

[2] A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Department's ability to initiate, authorize, record, process, or report financial data reliably in accordance with U.S. generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Department's consolidated financial statements that is more than inconsequential will not be prevented or detected by the Department's internal control over financial reporting. A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis.

[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] Beginning in FY 2007 the activities and balances of the WCF, previously reported separately, have been included in the financial statements of the OBDs.