A meeting of the Federal Prison Industries, Inc. (FPI) Board of Directors was held on April 17, 2024, via teleconference.

IN ATTENDANCE:

David Spears, Chairman
Donald R. Elliott, Vice Chairman
Lee Lofthus, Member
Dee Reardon, Member

QUORUM: A quorum was present.

ALSO IN ATTENDANCE:

William Lothrop, Deputy Director, Federal Bureau of Prisons
Patrick T. O'Connor, Chief Executive Officer, FPI
Sean Marler, Deputy Assistant Director, FPI
Marianne Cantwell, General Counsel, FPI
Edward Porras, Chief Financial Officer, FPI
Valery Logan, Executive Assistant, FPI

Chairman Spears opened the meeting.

Deputy Director Lothrop provided an update on Federal Bureau of Prisons (Bureau) issues impacting FPI.

I. Chief Executive Officer's Report

Mr. O'Connor provided an update on his recent travel activities since the last Board meeting, which included attending the Principles of Leadership 2 course, the Vision Expo, visits to several institutions, and participation in a Warden's conference. He also highlighted the issuance of the audit restatement letter on April 3rd, informing Congress and relevant agencies that the FY21 and FY22 audits were being taken down for restatement. The letters were distributed to all necessary parties, and there have been no significant responses. The restated audits will be ready for reissuance soon.

Mr. O'Connor discussed the current challenges of MIPRs in the Electronics Business Group. He provided a status of efforts to resolve.

Mr. O'Connor discussed the ongoing challenge with the slow deliveries of GSA vehicles, noting that while there has been some month-to-month improvement, the overall pace has not met expectations, leading to a significant backlog of outstanding vehicles.

He highlighted a positive development regarding the Department of Defense's (DoD) DIBS system, which previously prevented FPI from bidding on certain jobs due to FPI being classified as a government entity rather than a manufacturer on sam.gov. After more than six months of effort, an exemption has now been secured that allows FPI to access the necessary technical documentation and bid on jobs, which should improve deal flow.

Mr. Elliott inquired whether this issue with the DIBS system was new and if FPI had previously been able to bid on such work. Mr. O'Connor clarified that the issue arose after system updates were made. The problem took time to resolve due to a miscommunication between different agencies, each expecting the other to make the necessary changes. The DoD ultimately made the needed adjustments to resolve the issue.

Mr. O'Connor outlined a challenge related to security issues, noting that the closure of FCI Dublin has required the transfer of call center operations from FCI Dublin to FPC Bryan and FCI Tallahassee. However, not all operations may be moved due to differences in computer systems, and it will take a week or two to fully assess the impact. Mr. O'Connor also highlighted a broader increase in security concerns, particularly with the rise of incidents involving drones and fentanyl. This has led to more frequent shakedowns and shutdowns across facilities. While the Wardens have generally been effective in quickly restoring operations, these security measures are still causing disruptions that need to be managed moving forward.

Mr. O'Connor discussed concerns regarding the budget, particularly related to the Bureau and other contracts affected by delays in appropriations and spending bills this year. He indicated that the delay in contract releases by the Defense Logistics Agency (DLA), due to funding delays, could result in less overlap with new contracts, potentially causing issues in the latter half of the year. The BOP is also facing budget struggles, which may lead to a reduced influx of year-end orders for inmate clothing and mattresses, typically placed by wardens and regions.

Mr. Elliott inquired about the potential impact of these budget issues on the organization moving forward. Mr. O'Connor responded that while the DLA contracts should be relatively stable, there might be lean times in the last quarter of this fiscal year. He noted that inflation and military budget constraints could create further difficulties, especially as more budget funds are allocated to items FPI does not produce.

Mr. Elliott asked if the financial impact of these challenges could be quantified to avoid surprises at the end of the year. Pat mentioned that while he does not foresee a significant impact on the current fiscal year, there may be implications for the first quarter of the next fiscal year. He agreed to begin gathering information to estimate the potential impact, noting that more accurate forecasts would be available after DLA's annual meeting, where they provide projections for the coming year. Mr. Elliott confirmed that once the necessary information is available, a report should be put together for the Board assessing the potential financial impact.

Mr. O'Connor informed the Board that despite new orders currently running ahead of last year's bookings, he anticipates that the typical end-of-year influx will be reduced.

On a positive note, Mr. O'Connor highlighted the significant improvement in cybersecurity within FPI's Management Information Systems Branch (MISB). Previously ranked last among 27 groups in the Department of Justice's cybersecurity posture report, we have now moved up to number 10, thanks to extensive upgrades to computers for adults in custody (AICs).

Mr. O’Connor provided an update on key performance indicators. He reported that FPI has met its fiscal year (FY) 2024 target of full-time AICs employed with approximately 10,648 full-time equivalent AICs working daily. However, the number of FPI AICs within three years of release has decreased significantly, largely due to early releases during the pandemic. This trend, coupled with AICs close to release focusing on earning time credits through various programs, has made it more challenging to maintain consistent participation in work programs. Mr. O’Connor noted that FPI is evaluating whether this metric remains effective or if a new measure is needed.

Mr. O’Connor reported that FPI’s year-to-date (YTD) revenue was $219.7 million, missing the FY24 YTD target by just $400,000 but $1.5 million above FY23 YTD figures. Net income significantly improved, at $17.9 million, a $23 million increase from FY23’s YTD loss. This was boosted by higher interest income and positive operating margins.

Control charts show most metrics within target, with net profits exceeding expectations and selling expenses reduced due to a fuel surcharge and a successful transition in logistics companies, positively impacting the Office Furniture Group (OFG).

Customer performance improved with on-time deliveries up from last year, though still below the FY24 target. The backlog is at $303 million to maintain factory utilization. However, defect rates have risen due to increased part-time work, prompting a need for more training.

Finished goods inventory turns improved to nearly 5, up from 4.4 last year.

Lost hours were significantly reduced, thanks to effective management, and the AIC workforce is operating at 90% of pre-pandemic levels.

II. Financial Update

Mr. Porras provided an update on FPI’s financials. FPI has had net gains since November. During March, FPI had a net gain of $4.8 million. The major drivers were:

- Sales were lower than plan by $2 million.
- Cost of sales (COS) was 72%, compared with 74% in February and 78% in January.
- Operational income is positive this month at $2.9 million.
- Investment income had a gain of $1.8 million.

Selling expenses have a credit balance of $850,000 due to the collection of fuel surcharge fees that had not been automatically invoicing. Variances in selling expenses will continue to occur due to destination pricing of products being an estimate of freight costs and not an exact quote.

Year to date, FPI has a net gain of $17.9 million. Sales are lower than plan by $400,000. YTD COS is at 77%, which is $1 million below plan. Operational income is positive this period at $6.8 million. FPI’s YTD investment income is $8.8 million, and other income is $2.2 million. These results are mainly driven by COS being 3.175% below plan and selling expenses having a credit balance of $850,000 in March.

YTD total sales are at $214 million. YTD total COS are at $168 million.

FPI’s YTD revenues from services we provide to clients are lower than plan by $650,000 but higher than last year.

Actual overhead costs at the factory level are $62 million. The applied overhead is under applied by $17 million. We take into consideration that not all locations applied overhead. The under applied overhead is adjusted each period using the Capitalization of Overhead Entry, adjusting our inventory. Our general and administrative expenses (G&A) are lower than plan by $6 million.

We are in phase 3 of our revenue recognition implementation. We are in the process of updating our warehouse procedures policy, which includes training implementation.

FPI ended March with $222 million in available cash. Accounts Receivable are at $41 million. Our inventory is at $138 million, up from $129 million in January.

III. Action Items/Legal Updates

The Board unanimously approved the draft meeting minutes from the February 2024 Board meeting. The Board discussed potential dates for the next Board meeting.

Ms. Cantwell provided an update on recent legal and legislative matters.

The meeting adjourned. /s/

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Lee Lofthus, Interim Assistant Director/CEO