



BUREAU OF ALCOHOL, TOBACCO, FIREARMS AND EXPLOSIVES ANNUAL FINANCIAL STATEMENTS FISCAL YEAR 2012

U.S. Department of Justice
Office of the Inspector General
Audit Division

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January 2013

**BUREAU OF ALCOHOL, TOBACCO,
FIREARMS AND EXPLOSIVES
ANNUAL FINANCIAL STATEMENTS
FISCAL YEAR 2012**

**OFFICE OF THE INSPECTOR GENERAL
COMMENTARY AND SUMMARY**

This audit report contains the Annual Financial Statements of the Bureau of Alcohol, Tobacco, Firearms and Explosives (ATF) for the fiscal years (FY) ended September 30, 2012, and September 30, 2011. Under the direction of the Office of the Inspector General (OIG), Cotton & Company LLP performed ATF's audit in accordance with auditing standards generally accepted in the United States of America. The audit resulted in an unqualified opinion on the FY 2012 financial statements. An unqualified opinion means that the financial statements present fairly, in all material respects, the financial position and the results of the entity's operations in conformity with U.S. generally accepted accounting principles. For FY 2011, ATF also received an unqualified opinion on its financial statements (OIG Report No. 12-14).

Cotton & Company LLP also issued reports on internal control over financial reporting and on compliance and other matters. The auditors identified one significant deficiency in internal control in the FY 2012 *Independent Auditors' Report on Internal Control over Financial Reporting*. The significant deficiency related to weaknesses in review and oversight of financial reporting. Specifically, ATF needs to improve internal controls over cash, monetary instruments, and other properties seized for evidence, and year-end unfilled customer order balances to ensure the accuracy of its financial statements.

No instances of non-compliance or other matters that are required to be reported under *Government Auditing Standards* were identified during the audit in the FY 2012 *Independent Auditors' Report on Compliance and Other Matters*. Additionally, Cotton & Company LLP's tests disclosed no instances in which ATF's financial management systems did not substantially comply with the *Federal Financial Management Improvement Act of 1996*.

The OIG reviewed Cotton & Company LLP's reports and related documentation and made necessary inquiries of its representatives. Our review, as differentiated from an audit in accordance with *Government Auditing Standards*, was not intended to enable us to express, and we do not

express, an opinion on ATF's financial statements, conclusions about the effectiveness of internal control, conclusions on whether ATF's financial management systems substantially complied with the *Federal Financial Management Improvement Act of 1996*, or conclusions on compliance with laws and regulations. Cotton & Company LLP is responsible for the attached auditors' reports dated November 5, 2012, and the conclusions expressed in the reports. However, our review disclosed no instances where Cotton & Company LLP did not comply, in all material respects, with auditing standards generally accepted in the United States of America.

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Management's Discussion and Analysis

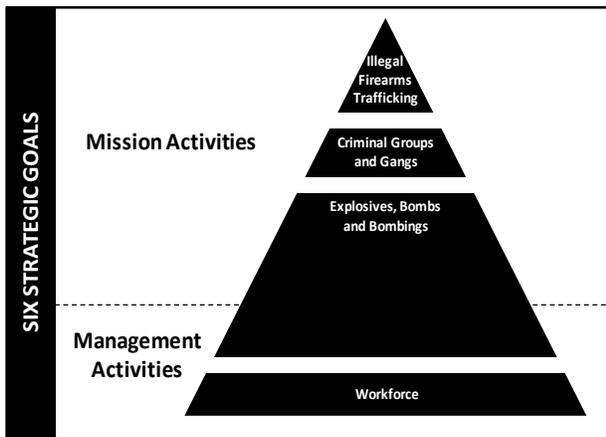
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U. S. Department of Justice
Bureau of Alcohol, Tobacco, Firearms and Explosives
Management's Discussion and Analysis
Unaudited

MISSION

The Bureau of Alcohol, Tobacco, Firearms and Explosives (ATF or the Bureau) is a law enforcement organization within the U.S. Department of Justice (DOJ). ATF is dedicated to the reduction of violent crime, prevention of terrorism, and protection of our Nation. ATF investigates and prevents crimes that involve the unlawful manufacture, sale, possession and use of firearms and explosives; acts of arson and bombings; and illegal trafficking of alcohol and tobacco products. ATF regulates the firearms and explosives industries from manufacturing and/or importation through retail sale. We screen and license entities that engage in commerce in these commodities, and specify the form and content of their business records. In the case of explosives, we have established standards for the safe storage of materials to which licensees must adhere.



ATF groups its activities into 10 core functions. Through these core functions ATF reduces violent crime by enforcing Federal laws and regulations related to firearms, criminal groups and gangs, explosives, arson, alcohol and tobacco.

ATF's Strategic Plan for 2010 – 2016 defines six of its core functions as strategic goals; four core mission activities and the two core management activities. The mission goals in illegal firearms trafficking, criminal organizations, explosives, and fire/arson reflect our core areas of expertise, which

we consistently work to strengthen. The management goals — modernizing our organization and managing our workforce — will support our mission and ensure its successful accomplishment. The management framework focuses on strategic planning, budgeting, performance measurement, and Bureau operations.

Mission Activities:

- **Strategic Goal - Illegal Firearms Trafficking:** Reduce violent firearms crimes by strengthening firearms trafficking intelligence gathering, analysis, inspection, and investigative activities.
- **Strategic Goal - Criminal Groups and Gangs:** The prevalence of criminal groups and gangs requires strategies to make our communities safer by expanding our efforts to identify, target, and dismantle those criminal gangs and organizations that utilize firearms, arson, explosives and alcohol and tobacco diversion in furtherance of violent criminal activity.

- **Strategic Goal - Explosives, Bombs and Bombings:** Advance domestic and international explosives expertise to prevent, detect, and investigate acts of violent crime and terrorism and to enhance public safety.
- **Strategic Goal - Fire and Arson:** Advance the science of fire investigation globally, by setting and delivering the highest standards in response, research, information sharing, and training.

Management Activities:

- **Strategic Goal - Modernization:** Modernize business processes and systems for improved information sharing, knowledge management, and use of innovative technologies to support ATF's critical mission.
- **Strategic Goal - Workforce:** Attract, develop, and retain an expert workforce to execute the ATF mission in the emerging business environment.

VISION

We Are ATF - A dedicated team securing America's future by accomplishing a critical mission today.
 We Protect America.
 We Protect Your Community.

VALUES

We value our people and those we serve.
 We value professionalism, integrity, diversity, commitment, innovation, and excellence.
 We value partnerships that promote the safety of our communities.

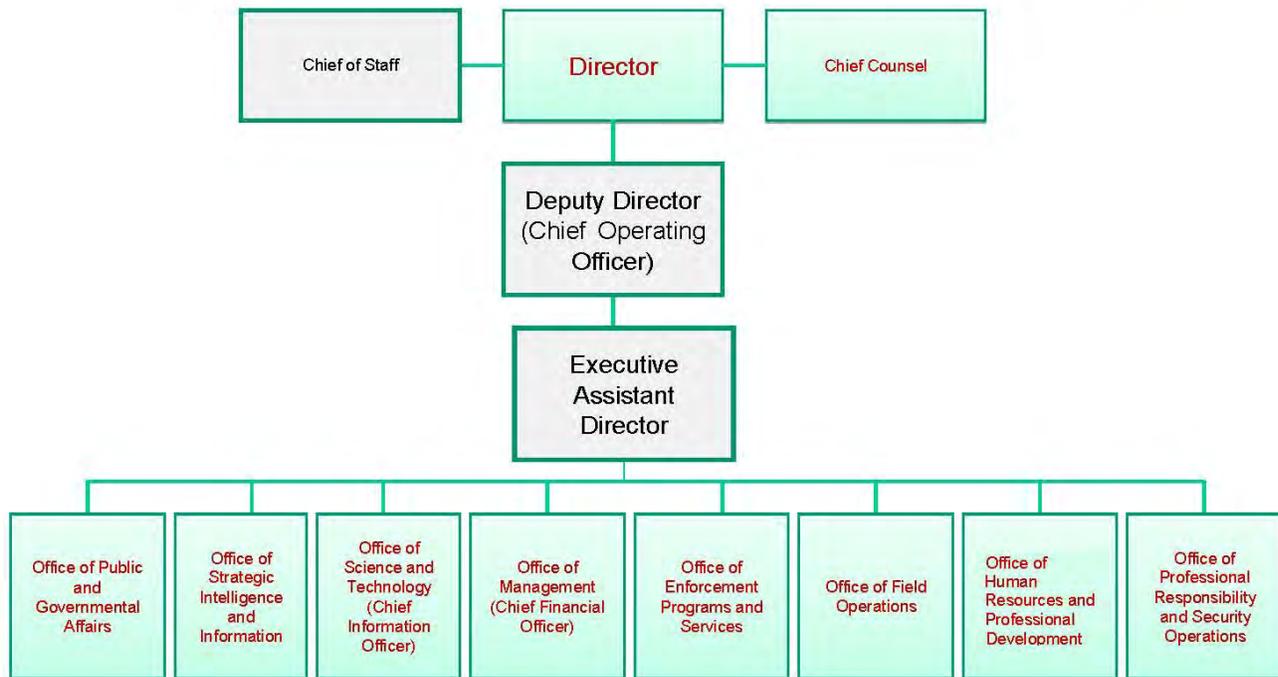
ORGANIZATIONAL STRUCTURE

ATF's national headquarters, located in Washington, DC, includes offices that develop major policies and programs in accordance with the applicable laws and regulations that ATF enforces. ATF's executive structure consists of the Director, Deputy Director, Executive Assistant Director, Chief Counsel, Chief of Staff, and the Assistant Directors for Field Operations; Enforcement Programs and Services; Strategic Intelligence and Information; Professional Responsibility and Security Operations; Public and Governmental Affairs; Management; Science and Technology/Chief Information Officer; and Human Resources and Professional Development. These executives form the Bureau's Strategic Leadership Team, which oversees and approves large investments such as buildings, relocations, information technology (IT) investments, and equipment. The Offices of the Chief of Staff, Ombudsman, Equal Opportunity, and Strategic Management, and the Disclosure Division are key components of the Office of the Director.

ATF has offices throughout the United States, including Puerto Rico, the Virgin Islands and Guam. ATF also has a presence at U.S. embassies in El Salvador, Colombia, Mexico, and Canada; U.S. Consular offices in Tijuana, Ciudad Juarez, Guadalajara and Monterrey, Mexico; Interpol Headquarters in Lyon, France; and at Europol in The Hague, Netherlands, to address the trafficking of firearms, explosives, alcohol, and tobacco. The field structure is comprised of 25 field divisions strategically located throughout the United States, with a single executive heading each office and having responsibility for all law enforcement and industry regulation within the geographical area.

ATF ORGANIZATION CHART

Bureau of Alcohol, Tobacco, Firearms and Explosives



FINANCIAL STRUCTURE

ATF's primary funding source is an annual appropriation, which funds salaries, operating expenses, property and equipment, as authorized by law. ATF may also receive appropriations to cover specific needs, such as expenses incurred as the result of the relocation of law enforcement frequencies in the radio spectrum. However, these appropriations are situational in nature and occur as the need arises. In addition, ATF has agreements with other Federal entities, including the Department of Justice Assets Forfeiture Fund, to reimburse authorized ATF expenses.

ATF's central budget office formulates, allocates and executes all funding among the directorates. The Budget Branch (BB) interprets all Treasury, Government Accountability Office (GAO), Office of Management and Budget (OMB) and General Services Administration (GSA) regulations relevant to budget formulation and execution. In addition, the BB directs the procedures for formulation, presentation and execution of the Bureau's budget. Other responsibilities include:

- Performs apportionment and allocation of funds;
- Performs continual analyses of the Bureau's financial posture;
- Prepares budget integration of short and long-term program planning, reprogramming and reapportioning of funds;
- Prepares the formal budget submissions to the Department, OMB, and the Congress for approval;
- Prepares briefings for top management on all budget presentations for formal hearings and annual/mid-year reviews of allocations;
- Initiates supplemental and amendments to the budget based on program requirements;
- Maintains historical budget files and workload statistics; and
- Supports the orderly allocation of human resources through internal position ceilings.

ANALYSIS OF FINANCIAL STATEMENTS

ATF prepares the principal financial statements required by OMB Circular A-136, *Financial Reporting Requirements* and the DOJ Financial Statement Requirements and Preparation Guide.

The Consolidated Balance Sheet is a presentation of ATF's assets, liabilities, and net position as of the end of the fiscal year. Assets represent the amounts of future economic benefits that are owned or managed by the Bureau. Liabilities are the amounts that are owed by the Bureau and net position comprises the unexpended appropriations and the cumulative results of operations.

Total assets as of September 30, 2012 and 2011, were \$550.4 and \$556.7 million, respectively with a decrease of approximately 1.1 percent. The Fund Balance with the Treasury represents approximately 42.3 percent of assets in FY 2012 and 43.4 percent in FY 2011.

Total liabilities as of September 30, 2012 and 2011, were \$356.5 million and \$352.3 million, respectively. The increase of \$4.2 million or 1.2 percent is primarily due to an increase in liabilities from project-generated proceeds of \$1.2 million and an increase in the FECA Actuarial Liability of \$6.3 million as well as an overall decrease in accounts payable of \$3.5 million.

The Consolidated Statement of Net Cost presents the gross operating costs and any related exchange revenue for the reporting period. The bottom line is the net cost to operate and run the Bureau programs for the fiscal year. ATF records the full cost of all transactions, including imputed costs absorbed by other entities. The net costs of operations as of September 30, 2012 and 2011 were \$1,203.7 million and \$1,182.4 million, respectively, an increase of approximately \$21.3 million.

The Consolidated Statement of Changes in Net Position presents both the net cost of operations and how those costs were financed, whether from appropriations, transfers, or imputed financing. Unexpended appropriations as of September 30, 2012 and 2011 were \$175.1 million and \$174.2 million, respectively. The increase is approximately 0.5 percent. The Net Position as of September 30, 2012 and 2011 was \$193.9 million and \$204.4 million, respectively, with a decrease of approximately 5.1 percent. The FY 2012 appropriations increased by \$37.2 million or 3.3 percent.

The Combined Statement of Budgetary Resources presents how resources are received by ATF, whether through appropriations, other authorities, or reimbursements and recoveries. The Combined Statement of Budgetary Resources also provides the status of those resources, including the amounts that are obligated, and whether the source of those obligations is direct or reimbursable funds. Obligations incurred as of September 30, 2012 and 2011 were \$1,279.3 million and \$1,260.4 million respectively, or an increase of approximately 1.5 percent.

The Combined Statement of Custodial Activity presents non-exchange revenue consisting of fees and licenses that ATF collects and distributes and proceeds from undercover operations. Non-exchange revenues are unavailable for use by ATF and are transferred to the General Fund of the Treasury. The primary sources of these collections are firearms and explosive licenses and import fees. The total custodial revenue as of September 30, 2012 and 2011 was \$24.7 million and \$21.5 million, respectively. The increase of approximately 15.0 percent is primarily due to an increase in the application volume and related payments, for National Firearms Act (NFA) transfers and/or registration of NFA class weapons.

**Table 1. Source of ATF Resources
(Dollars in Thousands)**

Source	FY 2012	FY 2011	Change%
Earned Revenue	\$ 81,369	\$ 91,300	-11%
Budgetary Financing Sources			
Appropriations Received	1,152,000	1,114,772	3%
Appropriations Transferred-In/Out	(15,067)	(7,892)	91%
Other Adjustments and Other Budgetary Financing Sources	-	(2,231)	-100%
Other Financing Sources			
Transfers-In/Out Without Reimbursement	15,949	3,153	406%
Imputed Financing from Costs Absorbed by Others	40,346	47,544	-15%
Total	\$ 1,274,597	\$ 1,246,646	2%

**Table 2. How ATF Resources are Spent
(Dollars in Thousands)**

Strategic Goal (SG)	FY 2012	FY 2011	Change%
SG 1: Prevent Terrorism and Promote the Nation's Security Consistent with the Rule of Law			
<i>Net Cost</i>	\$ 6,419	\$ 5,649	14%
SG 2: Prevent Crime, Protect the Rights of the American People, and Enforce Federal Law			
Gross Cost	1,278,676	1,268,049	
Less: Earned Revenue	81,369	91,300	
<i>Net Cost</i>	1,197,307	1,176,749	2%
Total Gross Cost	1,285,095	1,273,698	
Less: Total Earned Revenue	81,369	91,300	
Total Net Costs of Operations	\$ 1,203,726	\$ 1,182,398	2%

2012 Financial Highlights

ATF activities primarily support the Department's goal to Prevent Crime, Protect the Rights of the American People, and Enforce Federal Law. However, many of our core activities, including ATF participation on task forces to prevent terrorism, also support the Department's goal to Prevent Terrorism and Promote the Nation's Security Consistent with the Rule of Law.

Strategic Goal 1: Prevent Terrorism and Promote the Nation's Security Consistent with the Rule of Law, 0.5 percent of ATF's net costs support this Goal, which includes ATF activity in the Joint Terrorism Task Force and the Terrorist Device Analysis Center. The Goal 1 net costs for FY 2012 and FY 2011 were \$6.4 million and \$5.6 million, respectively, an increase of \$.8 million or approximately 13.6 percent.

Strategic Goal 2: Prevent Crime, Protect the Rights of the American People, and Enforce Federal Law, 99.5 percent of ATF's net costs support this Goal, which includes all ATF activities except those reported in Strategic Goal 1. The Goal 2 net costs for FY 2012 and FY 2011 were \$1,197.3 million and \$1,176.7 million, respectively, an increase of approximately 1.8 percent. This increase is not material in nature.

PERFORMANCE INFORMATION

Data Reliability And Validity

ATF views data reliability and validity as critically important in the planning and assessment of performance. As such, this document includes a discussion of data validation, verification, and any identified data limitations for each performance measure presented. ATF ensures that data reported meets the following criteria:

At a minimum, performance data are considered reliable if transactions and other data that support reported performance measures are properly recorded, processed, and summarized to permit the preparation of performance information in accordance with criteria stated by management. Performance data need not be perfect to be reliable, particularly if the cost and effort to secure the best performance data possible will exceed the value of any data so obtained.

ATF Performance Measurement Discussion:

ATF has developed a Performance Index to link core functions to strategic goals and measure performance. ATF's outcome-based performance goal statements are shown below:

<i>Core Function</i>	<i>Performance Goal Statement</i>
Illegal Firearms Trafficking	Reduce the risk to public safety caused by illegal firearms trafficking
Firearms Criminal Possession and Use	Reduce the risk to public safety caused by criminal possession and use of firearms
Firearms Industry Operations	Improve public safety by increasing compliance with Federal laws and regulations by firearms industry members
Criminal Groups and Gangs	Reduce the risk to public safety caused by criminal organizations and gangs
Explosives, Bombs, and Bombings	Reduce the risk to public safety caused by bombs and explosives
Explosives Industry Operations	Improve public safety by increasing compliance with Federal laws and regulations by explosives industry members
Fire and Arson	Reduce the risk to public safety caused by the criminal use of fire
Alcohol and Tobacco	Reduce the loss of tax revenues caused by contraband alcohol and tobacco trafficking
Modernization	Modernize business processes and systems for improved mission effectiveness and transparency
Workforce	Attract, develop, and retain an expert workforce to execute the ATF mission

Each performance goal statement aligns with strategic objectives and corresponding performance indicators. ATF has established a target for each performance indicator in the Index based on historic performance and ATF's current or anticipated operating environment. Performance indicators are assigned weights based on their effectiveness in meeting objectives. The weight of each strategic objective is the sum of the weights of the performance indicators that comprise it. The performance goal statements are weighted based on budget decision unit (e.g., the impact of interdicting and preventing illegal firearms trafficking on ATF's firearms program decision unit), and ATF's current capabilities in the area of the performance goal statement. Weights are assigned to ATF's budget decision units (firearms, arson and explosives, and alcohol and tobacco) in accordance with established Congressional reprogramming thresholds among these mission areas. A more detailed explanation of ATF's Performance Index can be found in ATF's Strategic Plan or Congressional Budget Request at <http://atf.gov/publications/general/strategic-plan/>. ATF's Internet site contains supporting documentation and reference materials on ATF programs (<http://www.atf.gov>).

FY 2012 REPORT ON SELECTED RESULTS

STRATEGIC GOAL 2: Prevent Crime, Protect the Rights of the American People, and Enforce Federal Law, 99.5% of ATF's Net Costs support this goal.

PROGRAMS: Illegal Firearms Trafficking; Firearms Criminal Possession and Use; Criminal Groups and Gangs; Firearms Industry Operations

Background/Program Objectives: Violent firearms crime remains a significant and complex domestic problem, fueled by a variety of causes that vary from region to region. The common element, however, is the relationship between firearms violence and the unlawful diversion of firearms out of commerce into the hands of prohibited persons. ATF's unique statutory responsibilities and assets, including technology and information, are focused under the agency's Integrated Violence Reduction Strategy (IVRS) to remove violent offenders, including gang members, from our communities; keep firearms from those who are prohibited by law from possessing them; discourage, prohibit, and interrupt illegal weapons transfers in accordance with the law; and prevent firearms violence through community outreach.

Our firearms trafficking interdiction strategy complements our continued focus on the deployment of resources to specific localities where there is a high incidence of gang and gun violence. Through firearms trafficking interdiction efforts, ATF decreases the availability of illicit firearms and recommends for prosecution those who illegally supply firearms to prohibited possessors. Violent gang members are often involved in firearms trafficking, both for potential profit and in furtherance of drug trafficking and other crimes. The violence fueled by firearms trafficking is demonstrated in the crisis on our Southwest Border. Recent trends have shown an increase in the number of firearms recovered in Mexico, and these firearms fuel the growing violence along the border, including the brutal murders of hundreds of law enforcement officers and government officials. ATF's efforts to reduce violent firearms crime include:

- Implementing the ATF Southwest Border initiative which is a focused subset of ATF's broader firearms trafficking initiative, addressing U.S. based firearms trafficking that is fueling the violence along the Southwest Border and nationwide. The tracking of firearms attacks the prevalence of illegal firearms available in the Southwest Border region and stems the flow of firearms to criminal organizations in Mexico. Additionally, ATF enhances its efforts along the Southwest Border with an integrated violent crime and gang reduction program with initiatives like the Violent Crime Impact Teams and Regional Area Gang Enforcement Teams.
- Partnering with law enforcement agencies and prosecutors at all levels to develop focused strategies to investigate, arrest, and prosecute violent offenders, persons prohibited from possessing firearms, domestic and international firearms traffickers, violent gangs, and others who attempt to illegally acquire or misuse firearms.
- Assisting the law enforcement community in identifying firearms trafficking trends and resolving violent crimes by providing automated firearms ballistics technology, tracing guns used in crimes, and developing advanced firearms investigative techniques.

- Ensuring that only qualified applicants who meet the eligibility requirements of the law enter the regulated firearms industry by employing appropriate screening procedures prior to licensing.
- Inspecting firearms dealers to identify any illegal purchases or diversion of firearms to criminals and to ensure the accuracy of records used in tracing firearms. ATF ensures that firearms industry members comply with the Gun Control Act, the National Firearms Act, and the Arms Export Control Act.
- Keeping restricted firearms such as machine guns out of the hands of prohibited persons by performing criminal records checks on applicants. ATF maintains the accuracy and integrity of the National Firearms Registration and Transfer Record so that the location and ownership of restricted firearms are kept current.
- Ensuring that only firearms that are legally importable under ATF and State Department rules are imported into the United States and are properly marked and recorded by the importer for sale domestically.
- Collaborating with schools, law enforcement agencies, community organizations, and the firearms industry to implement educational programs which help to reduce firearms violence.
- Informing the public and firearms industry about ATF policies, regulations, and product safety and security, so that they can better comply with the law. To do so, ATF uses a variety of communication methods such as the Internet, trade and community publications, seminars, webinars, and industry meetings.

The following represent examples of ATF's success in support of Strategic Goal 2:

- In FY 2012, ATF collected approximately \$21.4 million in license fees, registration fees, Special Occupational Tax Stamps, and National Firearms Act taxes. This amount does not include fines, penalties and restitutions and is net of refunds.
- In FY 2012, ATF recommended 10,684 criminal cases against 17,405 defendants for prosecution – 1,466 of those cases involve 4,081 defendants engaged in gang related criminal conduct. Of the defendants recommended for prosecution, nearly 61% are previously convicted felons and 84% have prior arrest records.
- In FY 2012, ATF arrested 8,841 defendants, obtained 10,311 indictments and had prosecutions that resulted in 7,160 convictions. As a result, 6,204 defendants were sentenced to prison in FY 2012 including 50 defendants who received life sentences and 11 who received death sentences.
- In FY 2012, we initiated the following criminal investigations:
 - 25,589 firearms cases, including illegal possession and firearms trafficking;

- 2,784 arson and explosives cases, including bombing and attempted bombing cases; and
- 84 alcohol and tobacco diversion cases.
- In FY 2012, ATF seized 791 firearms and 635,783 rounds of ammunition destined for the Southwest Border. In FY 2012, ATF arrested 229 defendants and obtained evidence that these defendants were accountable for 9,357 firearms believed to have been trafficked in cases related to the Southwest Border.
- In FY 2012, ATF referred 211 cases involving 534 defendants for prosecution related to the Southwest Border.
- In FY 2012, there were 7,804 retail dealers and pawnbrokers who held Federal Firearms Licenses (FFLs) along the Southwest Border in Texas, Arizona, New Mexico, and Southern California. In 2012, ATF inspected 4,130 or 53 percent of the FFLs in those four states.

ATF's Internet site contains supporting documentation and reference materials on ATF programs. It can be accessed at <http://www.atf.gov>.

Performance Measurement

DOJ Priority Goal (New Measure): Percentage Increase in Gang Arrests Resulting from Coordination of Gang Investigations

FY 2011 Baseline: 88 Arrests

FY 2012 Target: 2% Increase

FY 2012 Actual Performance: 16% Decrease (74 Arrests)

Data Definition: ATF's contribution to this measure will reflect the number of gang-related cases and arrests resulting from coordination with state and local law enforcement and supported by the Gang Targeting, Enforcement, and Coordination Center/Operational Section Gangs (GangTECC/OSG). ATF's data will be derived from performance data collected for firearms-related cases and is linked to ATF's performance goal to "Reduce the risk to public safety caused by criminal organizations and gangs." Examples of ATF-specific performance indicators linked to this goal include, the numbers of gang-related defendants referred and convicted, and the number of criminal group or gang-related defendants in cases that have the active involvement of state and local law enforcement partners.

Data Collection and Storage: The data source is ATF's National Field Office Case Information System (NFOCIS), which is ATF's integrated and centralized data management solution allowing real time monitoring and oversight of all criminal enforcement activities in the field.

Data Validation, and Verification: ATF's performance review process uses goal-focused, data-driven reviews to assure that follow-up steps are taken to increase the likelihood of achieving better outcomes and higher productivity. This same review process tracks ATF's progress in achieving its long-term and annual goals by showing long-term trends, along with contextual indicators and makes clear the link between agency output targets and longer-term outcome goals. The data are subsequently verified through ATF's inspection process, performed internally by the Office of

Professional Responsibility and Security Operations. The internal inspections occur on a four year cycle and are performed at each ATF field office and division.

Data Limitations: ATF investigations are often complex and time consuming in nature, and often span multiple years from initiation through closure. The case-related data is calculated based on the date investigations are closed, and is therefore likely to include investigations that have spanned previous time periods.

Discussion of FY 2012 Results:

ATF's contribution to DOJ's Priority Goal is 74 arrests, which is a 16 percent decrease from the FY 2011 baseline figure of 88. However, while the number of arrests is down, the total number of ATF cases coordinated through GangTECC has increased from 22 in FY 2011 to 108 in FY 2012. Approximately 70 percent of these cases were initiated during the 3rd and 4th quarters of FY 2012, and will result in arrests and referrals for prosecution during FY 2013. Inclusive of the cases coordinated through GangTECC, in FY 2012, 1,889 gang-related and 1,500 trafficking-related defendants in ATF cases were convicted. The following case highlights ATF's FY 2012 efforts:

Black Rain

In September 2008 the President of the San Francisco Chapter of the Hells Angels was murdered in a gang related incident in the Mission District of San Francisco. Pursuant to an extensive ATF investigation, a member of the Mongols Motorcycle Club was found guilty of murder in aid of racketeering, assault with a deadly weapon (in aid of racketeering), use of firearm during/in relation to a crime of violence, and using a firearm causing murder during a crime of violence. The jury found that he had murdered the President of the Hells Angels Chapter to maintain or increase his position in the Mongols Motorcycle Club. In May 2012, he was sentenced to four (4) life terms of imprisonment.

PROGRAMS: Explosives, Bombs, and Bombings; Explosives Industry Operations; Fire and Arson

Background/Program Objectives: ATF is the Federal agency primarily responsible for administering and enforcing the criminal and regulatory provisions of the Federal laws pertaining to destructive devices (bombs), explosives, and arson. Over nearly 40 years, ATF has developed investigative capabilities, expertise, and resources that have positioned ATF as this Nation's definitive source for explosives and fire investigative knowledge and assistance.

Approximately 99 percent of all bombings in the United States fall under the jurisdiction of ATF, but ATF also responds to and plays a key role in investigating the few incidents that are classified as "terrorist bombings." These include incidents that are classified as domestic terrorism, such as those perpetrated by animal rights activists. An array of specialized programs and technical services managed and executed by a diverse and knowledgeable workforce is the foundation of ATF's success. These include, but are not limited to, the following:

- **Certified Explosives Specialist (CES) Program:** The primary mission of this program is to protect the public through the vigorous enforcement of the Federal explosives laws; to provide credible explosives crime scene examinations; to lend expertise in support of security measures implemented at special events; and to assist ATF's law enforcement counterparts at the Federal, state, local, and international levels in their efforts to investigate complex explosives-related incidents.
- **Explosives Enforcement Officers:** ATF's explosives enforcement officers (EEOs) provide technical assistance and support in explosives matters. EEOs have extensive experience in explosives and bomb disposal. Most EEOs are former military explosive ordinance disposal (EOD) trained, with extensive training in nuclear, biological, chemical, and conventional high explosive and incendiary weapons systems. EEOs render explosive devices safe and/or disassemble explosive and incendiary devices, prepare destructive device determinations, and render expert testimony in support of such determinations in state and Federal criminal court proceedings. Additionally, EEOs provide expert analysis and onsite investigative technical assistance at bombing and arson scenes and scenes where explosions of an undetermined nature have occurred. They play a critical role in large-scale explosives destructions.
- **Certified Fire Investigator (CFI) Program:** The CFI Program consists of special agents who have undergone an extensive 2-year training program designed to educate them in the field of advanced fire scene examination, with emphasis on modern principles of fire dynamics. These agents comprise the only group of fire origin and cause specialists within the Federal sector.

The special agent CFIs serve as ATF's primary resource in fire-related matters. They conduct fire scene examinations and render origin and cause determinations on behalf of ATF; provide expert courtroom testimony; provide technical support and analysis to assist other special agents and prosecutors with court preparation, presentation of evidence, and technical interpretation of fire-related information; lend technical guidance in support of field arson investigative activities; conduct arson-related training for ATF special agents and other Federal, state, and local fire investigators; and conduct research and identify trends and patterns in fire incidents.

- **National Response Team (NRT):** ATF's National Response Team was formed in 1978 to help meet the needs of those who respond to and investigate complex incidents. The NRT consists of four regional response units. Each unit can respond to an incident within 24 hours and is comprised of technical experts and veteran special agents having post-blast and fire origin and cause expertise, including CESs, CFIs, EEOs, forensic chemists, fire protection engineers, and electrical engineers, with forensic mapping capabilities. ATF also utilizes canines with accelerant and explosives detection abilities. Further complementing the team's efforts are intelligence and audit support, and technical and legal advisors.

Performance Measurement

Selected Performance Goal Statement: Reduce the Risk to Public Safety Caused by Bombs and Explosives.

FY 2010 Performance Score 93
 FY 2011 Performance Score 96
 FY 2012 Target Score 73
 FY 2012 Actual Score 89

Linked Strategic Objective:

Continually address and mitigate emerging explosives and bombing threats by developing and implementing proactive regulatory and investigative tactics.

Linked Performance Indicators:

- Number of defendants convicted, in the given fiscal year, for violations related to explosives, regardless of the year of referral:
 - FY 2010 Performance 180
 - FY 2011 Performance 139
 - FY 2012 Target 180
 - FY 2012 Actual 128
- Number of defendants referred, in the given fiscal year, for prosecution for violations related to explosives:
 - FY 2010 Performance 351
 - FY 2011 Performance 401
 - FY 2012 Target 300
 - FY 2012 Actual 277
- Number of explosive destructions/disposals executed in the interest of public safety:
 - FY 2010 Performance 293
 - FY 2011 Performance 247
 - FY 2012 Target 350
 - FY 2012 Actual 290

- Number of explosives devices recovered:
 - FY 2010 Performance 325
 - FY 2011 Performance 446
 - FY 2012 Target 325
 - FY 2012 Actual 240

Linked Strategic Objective:

Lead the advancement of worldwide bombing and explosives expertise by conducting in-depth research and analysis and providing high quality training in all facets of explosives storage, detection, disruption, investigation and disposal.

Linked Performance Indicators:

- Number of people (ATF employees and Federal, state, local and international law enforcement) trained in explosives through the National Center for Explosives Training and Research:
 - FY 2010 Performance 1,259
 - FY 2011 Performance 1,713
 - FY 2012 Target 1,500
 - FY 2012 Actual 2,130
- Number of canine teams (ATF and Federal, state and local law enforcement) trained to meet the national odor recognition standard:
 - FY 2010 Performance 255
 - FY 2011 Performance 378
 - FY 2012 Target 350
 - FY 2012 Actual 344

Linked Strategic Objective:

Strengthen the detection, prevention, and investigation of explosives and bombing incidents through partnerships, collaboration, and comprehensive intelligence and information sharing.

Linked Performance Indicators:

- Number of active Bomb and Arson Tracking System (BATS) users (individuals):
 - FY 2010 Performance 5,227
 - FY 2011 Performance 7,164
 - FY 2012 Target 8,000
 - FY 2012 Actual 10,069
- Number of BATS accounts (agencies):
 - FY 2010 Performance 954
 - FY 2011 Performance 1,155
 - FY 2012 Target 1,300
 - FY 2012 Actual 1,649

Data Definitions: The sample measure reflects the outcome of ATF's investigative efforts in criminal explosives cases, from the initial on-scene assessment and determination that a crime has been committed, the application of technical and forensic resources in the course of the investigation, the identification of suspects, the development/gathering of evidence sufficient to support criminal charges, and finally, to the presentation of a criminal case suitable for prosecution to the prosecuting attorney. The measure also factors in the impact of training and collaboration with other law enforcement. As discussed on page 8, success in meeting a performance goal is calculated based on weights assigned to its supporting strategic objectives and their supporting performance indicators. Targets are established based on program priorities, historical performance and the anticipated operating environment.

Data Collection and Storage: Data to support the measure is collected through NFOCIS.

Data Validation and Verification: See **Data Validation and Verification** under firearms programs above.

Data Limitations: ATF investigations are often complex and time consuming in nature, and often span multiple years from initiation through closure. The case-related data is calculated based on the date investigations are closed, and is therefore likely to include investigations that have spanned previous time periods.

Discussion of FY 2012 Results:

ATF exceeded its performance score target. The following case examples highlight ATF's FY 2012 efforts in this area:

- In December 2008, a fire was reported at an apartment complex in Dallas, Texas. The fire caused significant damage to the complex, displacing numerous families. An origin and cause investigation determined the fire had been intentionally set. An ATF investigation developed information that an individual set the fire (and others) to obtain insurance proceeds and Red Cross victim assistance payments. Agents determined she was the head of an organized group of associates involved in starting fires for financial gain. Agents learned that she directed her associates on how and when to set fires, to obtain the greatest amount of victim assistance and insurance proceeds. She received a percentage of the monies collected. She and her associates were found to be responsible for starting 11 fires in the Dallas area, the final two causing nearly \$2 million in damage and significant Red Cross expenditures. In July 2010, the grand jury in Dallas returned a true bill against the subject and six associates, charges ranged from arson, wire fraud, use of fire to commit a felony and mail fraud. Her six associates pled guilty and were given sentences ranging from 37-46 months imprisonment and restitution of approximately \$3.8 million. In April 2012, she was sentenced to a 120-month term of imprisonment for wire fraud and a 120-month term of imprisonment for arson, to be served consecutively; she was ordered to pay approximately \$1.7 million.
- In May 2010, the Philadelphia Fire Department responded to a fire call at approximately 5:30 am at the business location owned by an individual who was outside of the country at the time of the

fire. An origin and cause investigation conducted by the ATF Arson Task Force indicated a “set fire”. A cooperator was developed pursuant to the investigation and he was engaged in multiple undercover contacts; search warrants were executed at the residence and new business location. In August 2011 a Federal complaint was issued against the suspect and he was arrested by ATF special agents. In March 2012, he was found guilty of an eight-count indictment (to include federal arson, conspiracy, mail fraud and obstruction of justice). A co-defendant was given a 90-month term of imprisonment; the main subject faces a 15-year minimum sentence in November 2012.

- In February 2004, a package bomb, exploded at the City of Scottsdale Arizona, Diversity & Dialogue Office. The package had been addressed to the Director of the office. He and two employees were injured in the explosion. ATF, the United States Postal Service and the Scottsdale Police Department initiated an investigation. Agents assigned to ATF subsequently developed two suspects, brothers, who were identified as white supremacists, affiliated with the White Aryan Resistance (WAR). Pursuant to a 5-year investigation involving numerous undercover meetings in Arizona, Illinois, Missouri and Oklahoma, wire intercepts and search warrants, the brothers were arrested on multiple charges, including conspiracy to damage a building by means of explosives, damaging a building by means of explosives and teaching to make or use an explosive or destructive device. In January 2012, one brother was found guilty of all three charges, he was subsequently sentenced to concurrent 40 year sentences; the other brother was found not guilty.

ANALYSIS OF SYSTEMS, CONTROLS, AND LEGAL COMPLIANCE

Federal Managers' Financial Integrity Act of 1982

The Federal Managers' Financial Integrity Act of 1982 (Integrity Act or FMFIA) provides the statutory basis for management's responsibility for and assessment of internal accounting and administrative controls. Such controls include program, operational, and administrative areas, as well as accounting and financial management. The Integrity Act requires Federal agencies to establish controls that reasonably ensure obligations and costs are in compliance with applicable law; funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and revenues and expenditures are properly recorded and accounted for to maintain accountability over the assets. The Integrity Act also requires agencies to annually assess and report on the internal controls that protect the integrity of Federal programs (FMFIA § 2) and whether financial management systems conform to related requirements (FMFIA § 4).

Guidance for implementing the Integrity Act is provided through OMB Circular A-123, *Management's Responsibility for Internal Control*. In addition to requiring agencies to provide an assurance statement on the effectiveness of programmatic internal controls and conformance with financial systems requirements, the Circular requires agencies to provide an assurance statement on the effectiveness of internal control over financial reporting. The Department requires components to provide both of the assurance statements in order to have the information necessary to prepare the agency assurance statements.

FMFIA Assurance Statement

ATF's Acting Director provided reasonable assurance that internal controls and financial systems met the objectives of Section 2 and 4 of the FMFIA and complies with the requirements of the Federal Financial Management Improvement Act (FFMIA).

ATF management has established and maintained effective internal control and financial management systems that meet the objectives of FMFIA. ATF assessed its internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations in accordance with OMB Circular A-123, as required by Section 2 of the FMFIA. Based on the results of this assessment, ATF provides reasonable assurance, as of September 30, 2012, that its internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations is operating effectively.

In accordance with Appendix A of OMB Circular A-123, ATF management conducted its assessment of the effectiveness of internal control over financial reporting, which included the safeguarding of assets and compliance with applicable laws and regulations. Based on the results of the assessment, ATF management can provide reasonable assurance that the ATF's internal control over financial reporting was operating effectively as of September 30, 2012, and the assessment identified no material weaknesses in the design or operation of the controls.

An update to the Appendix A assurance statement based on the results of third quarter testing performed as part of the CFO audit and OMB Circular A-123, identified issues in ATF's financial

reporting of cash, monetary instruments and other property seized for evidence processes. Management considers these deficiencies to be a reportable condition. ATF developed a Corrective Action Plan (CAP) to strengthen internal controls and oversight in the following areas:

- Improve existing policies and procedures to ensure the timely and accurate updating of property status in N-Force and agent responsibility to submit seized evidence currency to headquarters within five (5) business days of seizure.
- Develop standard operating procedures (SOP) for the movement of currency seized for evidence and the calculation of seized amounts to be recorded in the financial statements.
- Provide refresher agent training on seized property inventory and reconciliation procedures to ensure that they encompass validation of all property items in N-Force with status codes “in ATF’s custody”, “Release Requested”, “Release Pending”, “Destruction Requested” and “Destruction Pending”.
- Perform a complete book to floor and floor to book inventory with immediate reconciliation of differences.

ATF also assessed whether its financial management systems conform to government-wide requirements. Based on the results of this assessment, ATF provides reasonable assurance that there are no non-conformances that are required to be reported by Section 4 of the FMFIA. The testing did identify some deficiencies but the risks to the financial statements presented by these deficiencies were minimal and/or complementary or redundant controls evaluated achieved the same results.

ATF implements compensating controls to eliminate deficiencies and continues to identify system vulnerabilities and recommend security solutions to maintain systems at a reasonable assurance level. ATF bases this assertion on the following information sources:

- Internal control assessments including tests of key financial reporting controls;
- Management knowledge and experience gained from daily oversight of component programs, accounting systems, and administrative controls;
- Program audit reports;
- Financial statement audit reports;
- Financial management system evaluations and reports pursuant to OMB Circular A-127, *Financial Management Systems*;
- Evaluations and reports pursuant to the Federal Information Security Management Act (FISMA) and OMB Circular A-130, *Management of Federal Information Resources*;
- Management reviews;
- Internal reviews and investigations;
- Office of the Inspector General (OIG) reports and GAO reports;
- Performance plans and reports; and
- Statements of Assurance from each directorate head.

ATF’s accomplishments demonstrate the Bureau’s continued commitment to supporting a complex law enforcement mission of preventing terrorism, reducing violent crime, and protecting our Nation.

There is “reasonable assurance” that the financial system for ATF is in conformance with government-wide financial information standards and financial system functional standards under Section 4 of FMFIA for FY 2012.

This statement of assurance is based on the Unified Financial Management System (UFMS) which is the Bureau's core financial system for both revenue and administrative accounting, and assessments of all associated financial system modules. Based on the current management, operational, and technical controls in place, we have reasonable assurance that our financial and administrative systems have no material issues as they relate to Section 4 of FMFIA and are “compliant” with the FFMIA.

Some additional accomplishments related to Section 4 of FMFIA are as follows:

- ATF has consistently closed its books within three work days following an accounting period.
- ATF also utilizes an internal management tool for preparing accounting reconciliations and reporting financial information. To validate that procedures and policies are being followed, the tool monitors and manages budgeting and accounting activity and ensures that data in UFMS is current and accurate.

ATF controls that fulfill the Prompt Payment Act requirements include date stamping invoices by individuals not involved in the payment process; performing quality and validity reviews of each invoice; encouraging program offices to be prompt in entering receipts for goods and services into the financial system; and using management reporting tools to track outstanding invoices in the financial system to prevent late payments and associated interest penalties.

With respect to internal accounting control, ATF management identifies, designs, operates, maintains, and monitors an appropriate system of internal controls to enable the Bureau to accurately report its financial information to DOJ and meet the requirements of OMB Circular A-123, Appendix A and FFMIA.

In accordance with DOJ’s OMB Circular A-123 Implementation Plan, the Department’s Senior Assessment Team identified the business processes significant at the Departmental level and the DOJ components comprising a significant share of those processes. As required by the Department’s FY 2012 Guidance for Implementation of OMB Circular A-123, we have documented the following significant business processes and tested key controls for each:

- Information Systems;
- Budget/Funds Management;
- Financial Reporting;
- Property;
- Procurement;
- Seized and Forfeited Property and Currency; and
- Churning and Agent Cashier.

In addition, as also required by DOJ's FY 2012 Guidance for Implementation of OMB Circular A-123, ATF has tested key controls over sensitive payments related to:

- Travel Expenditures, including Premium Class and Executive Travel;
- Transit Subsidies; and
- Conference Expenditures.

The results of testing identified design or operational deficiencies in the above areas in ATF's internal controls over financial reporting as of September 30, 2012. However, these deficiencies are not considered to be reportable conditions. Management developed CAPs in each area to address deficiencies with plans to complete all milestones before the end of FY 2013.

Federal Financial Management Improvement Act of 1996

The FFMIA was designed to improve Federal financial and program managers' accountability, provide better information for decision-making, and improve the efficiency and effectiveness of Federal programs. FFMIA requires agencies to have financial management systems that substantially comply with Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Standard General Ledger (USSGL) at the transaction level. Furthermore, the Act requires independent auditors to report on agency compliance with the three requirements in the financial statement audit report. FISMA states that to be substantially compliant with FFMIA, there are to be no significant deficiencies in information security policies, procedures, or practices.

FFMIA Compliance Determination

During FY 2012, ATF assessed its financial management systems for compliance with FFMIA and determined that they substantially comply with FFMIA. This determination is based on the results of FISMA reviews and testing performed for OMB Circular A-123, Appendix A. Consideration was also given to any issues identified during the ATF's financial statement audit.

POSSIBLE FUTURE EFFECTS OF EXISTING EVENTS AND CONDITIONS

ATF has aligned its priorities to the current priorities of the President and the Nation to fight terrorism and to make our people and our communities safe from violence. Firearms and explosives are the primary tools of terrorism; ATF continues to regulate their legitimate use and enforce laws against criminal misuse. The illegal importation and trafficking of these terrorist tools continue to be disrupted through our investigations and regulatory efforts. Because our communities continue to struggle against the violence of criminals and gangs, ATF's initiatives and partnerships with other law enforcement organizations are critical components in the fight to protect the American people from violent firearms crime. ATF's partnership strategies with all of the U.S. Attorney's offices, including those in locations that currently do not have a full time Project Safe Neighborhood (PSN) resource, increase the effectiveness of efforts to target gangs and violent crime.

On August 29, 2011 the Office of Personnel Management (OPM) approved ATF's request to implement the Voluntary Early Retirement Authority (VERA) and Voluntary Separation Incentive Payment (VSIP) options. ATF requested this authority in order to address imbalances in our grade

structure and supervisor-to-employee ratios, to improve the ratio of Headquarters support positions to mission-focused field positions, and to drive the attrition necessary to position the Bureau to meet the challenges anticipated in the FY 2012 and FY 2013 budgets.

ATF established the initial VERA/VSIP application window of September 12 to October 14, 2011, during which time eligible employees could apply for the VERA/VSIP incentives. A total of 164 employees submitted retirement actions utilizing these incentives and all 164 separated from the Bureau by the November 30, 2011 deadline.

ATF continues to evaluate the impact of the departure of these employees in terms of both the goals of the VERA/VSIP program and the impact on ATF's expertise and overall capabilities.

The potential threat to public safety from criminal or terrorist theft and misuse of explosives cannot be overstated. Because of the extremely high and unacceptable risk, more comprehensive enforcement and regulatory efforts are essential to ensure the safe and secure storage of explosive materials. ATF's responsibility for public safety requires us to investigate all reported thefts of explosives and conduct comprehensive inspections of all explosives licensees triennially. ATF continues to work with the explosive industry manufacturers, importers, distributors, and users, as well as their associations, to improve the security, safe handling, and storage of these materials.

The following are examples of issues that have the potential to affect ATF operations in multiple regions:

- As gangs spread out across the United States, they may be moving to areas where ATF does not have a physical presence (e.g., increased violence on the Southwest Border that spills over into the United States from Mexico).
- In terms of workforce availability, cities that are experiencing dramatic increases in the cost of living will have difficulty providing rapid responses to emergency situations as personnel must travel long distances from residences; in addition, it may be difficult to retain qualified personnel in these areas.
- The potential closure of additional military bases, as well as large companies and industries that employ thousands of people in particular geographic areas, may cause crime to increase.
- Similarly, natural disasters such as hurricanes, floods and wildfires will present economic challenges and the potential for an increase in crime.
- Localities that are dealing with economic downturns and are having difficulty funding government services (e.g., police forces) will impact ATF operations, as local governments may not be able to provide officers to participate in ATF task forces.
- An economic downturn may lead to a rise in arson fires.
- Changes in state laws and changes in taxes have the potential to affect trafficking patterns (e.g., firearms, alcohol and tobacco).

- Several areas have expressed concern about the potential for violent acts by extremist environmental groups and organizations.
- Along with other agencies, ATF has contingency plans in place to continue operating if its own facilities and personnel are directly affected or threatened by terrorist acts. However, any such threats may have a negative impact on the Bureau's ability to address other forms of violence.
- Firearms manufacturers and distributors are reporting record high sales. The influx of firearms into commerce or into the hands of the general public may impact ATF.

IMPROPER PAYMENTS ELIMINATION AND RECOVERY ACT (IPERA) REPORTING

In accordance with OMB Circular A-123, Appendix C, *Requirements for Effective Measurement and Remediation of Improper Payments*, and the Departmental guidance for implementing the Improper Payments Elimination and Recovery Act (IPERA), the Department implemented a top-down approach to assess the risk of significant improper payments across all five of the Department's mission-aligned programs, and to identify and recapture improper payments through a payment recapture audit program. The approach promotes consistency across the Department and enhances internal control related to preventing, detecting, and recovering improper payments. Because of the OMB requirement to assess risk and report payment recapture audit activities by agency programs, the results of the Department's risk assessment and recapture activities are reported at the Department-level only.

In accordance with the Departmental approach for implementing IPERA, ATF assessed its activities for susceptibility to significant improper payments. ATF also conducted its payment recapture audit program in accordance with the Departmental approach. ATF provided the results of both the risk assessment and payment recapture audit activities to the Department for the Department-level reporting in the FY 2012 Performance and Accountability Report.

LIMITATIONS OF THE FINANCIAL STATEMENTS

- The financial statements have been prepared to report the financial position and results of operations of ATF, pursuant to the requirements of 31 U.S.C. 3515(b).
- While the statements have been prepared from the books and records of ATF in accordance with accounting principles generally accepted in the United States of America for Federal entities and the formats prescribed by OMB, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.
- The statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity.

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Independent Auditors' Reports

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INDEPENDENT AUDITORS' REPORT ON FINANCIAL STATEMENTS

Inspector General
United States Department of Justice

Acting Director
Bureau of Alcohol, Tobacco, Firearms and Explosives
United States Department of Justice

We have audited the accompanying Consolidated Balance Sheets of the Bureau of Alcohol, Tobacco, Firearms and Explosives (ATF), a component of the United States Department of Justice, as of September 30, 2012 and 2011, and the related Consolidated Statements of Net Cost, Consolidated Statements of Changes in Net Position, Combined Statements of Budgetary Resources, and Combined Statements of Custodial Activity for the years then ended. These financial statements are the responsibility of ATF's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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 (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, as amended. Those standards and OMB Bulletin No. 07-04 require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of ATF's internal control over financial reporting. Accordingly, we express no such opinion. 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.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the United States Department of Justice, Bureau of Alcohol, Tobacco, Firearms and Explosives as of September 30, 2012 and 2011, and its consolidated net costs, consolidated changes in net position, combined budgetary resources, and combined custodial activity for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

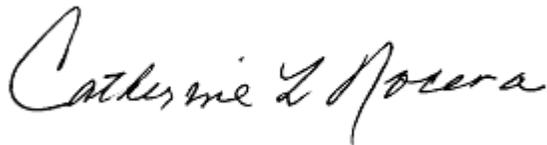
Accounting principles generally accepted in the United States of America and OMB Circular No. A-136, *Financial Reporting Requirements*, require that the *Management's Discussion and Analysis* and the *Combining Statements of Budgetary Resources* be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Federal Accounting Standards Advisory Board and OMB, who consider it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the

required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audits were conducted for the purpose of forming opinions on ATF's basic financial statements taken as a whole. The *Schedule of Spending* is presented for the purpose of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

In accordance with *Government Auditing Standards*, we have also issued our reports dated November 5, 2012, on our consideration of ATF's internal control over financial reporting and on our tests of its compliance with certain provisions of applicable laws and regulations. The purpose of those reports is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in assessing the results of our audits.

COTTON & COMPANY LLP

A handwritten signature in black ink that reads "Catherine L. Nocera". The signature is written in a cursive, flowing style.

Catherine L. Nocera, CPA, CISA
Partner

November 5, 2012
Alexandria, Virginia



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INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Inspector General
United States Department of Justice

Acting Director
Bureau of Alcohol, Tobacco, Firearms and Explosives
United States Department of Justice

We have audited the Consolidated Balance Sheets of the Bureau of Alcohol, Tobacco, Firearms and Explosives (ATF), a component of the United States Department of Justice (DOJ), as of September 30, 2012 and 2011, and the related Consolidated Statements of Net Cost, Consolidated Statements of Changes in Net Position, Combined Statements of Budgetary Resources, and Combined Statements of Custodial Activity for the years then ended, and have issued our report thereon dated November 5, 2012. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; 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. 07-04, *Audit Requirements for Federal Financial Statements*, as amended.

ATF's management is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our fiscal year 2012 audit, we considered ATF's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of ATF's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of ATF's internal control over financial reporting or on management's assertion on internal control included in *Management's Discussion and Analysis*. We limited our internal control testing to only those controls necessary to achieve the objectives described in *Government Auditing Standards* and OMB Bulletin No. 07-04. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*, such as controls relevant to ensuring efficient operations.

A deficiency in internal control 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. A material weakness is a deficiency, or combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the second paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described below, that, when combined, we consider to be a significant deficiency in internal control over financial reporting. A significant deficiency is a

deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit the attention by those charged with governance.

ATF's response to the finding identified in our audit is included after each recommendation. We did not audit ATF's response and, accordingly, we express no opinion on it.

FINANCIAL REPORTING CONTROLS NEED IMPROVEMENT (SIGNIFICANT DEFICIENCY) (NEW)

ATF's internal control over financial reporting needs improvement to ensure that amounts reported in its financial statements are valid, accurate, and complete. We identified errors and misstatements related to Cash, Monetary Instruments, and Other Property Seized for Evidence, and Year-End Unfilled Customer Order Balances, as discussed below.

CASH, MONETARY INSTRUMENTS, AND OTHER PROPERTY SEIZED FOR EVIDENCE

ATF's internal controls to ensure the accuracy, completeness, and reasonableness of its accounting for cash and monetary instruments (referred to as currency) and other property seized for evidence (non-valued firearms and vehicles) need improvement. ATF reports currency seized for evidence as Cash and Monetary Assets, along with a related liability. ATF also discloses information about currency, personal property with a value equal to, or exceeding \$1,000, and non-valued firearms seized for evidence in its financial statement footnotes. We noted the following control deficiencies:

ATF's Financial Reporting of Property Seized for Evidence Contained Errors

ATF's process for identifying and quantifying seized property balances is manual and subject to error. ATF uses the following to record seized currency balances and to prepare footnote disclosures:

- extracts from N-Force (N-Force Working Property Footnote Query reports [N-Force Query reports]);
- seized currency records maintained by the Asset Forfeiture and Seized Property Division (AFSPD); and
- the bank reconciliation for currency held in a Bank of America seized currency account.

ATF uses a suite of case and inspection management applications known as the National Field Office Case Information System (NFOCIS), which contains information on property seized for evidence. The Office of Strategic Intelligence and Information Systems (OSII) is responsible for maintaining NFOCIS and providing N-Force Audit Property and N-Force Vault reports (N-Force reports) and the N-Force Query reports to users, including the Accounting Branch.

We tested seized property balances at June 30, 2012, and determined that amounts reported were not accurate or complete, as follows.

- Amounts seized for 52 cases, totaling \$198,640, were recorded in N-Force as seized evidence in ATF's custody, but were not included in the seized currency general ledger account balance, and therefore, were not included in the financial statements and footnotes.
- Amounts seized for 13 cases were duplicated in the Accounting Branch's calculation of the seized currency balance (e.g., amounts that were in Headquarters' possession were also counted as seized currency held in the field), resulting in an overstatement of \$42,038 in the seized currency general ledger account balance.
- ATF's N-Force Query reports used to record seized currency account balances and financial statements disclosures are not complete. We compared the N-Force Query reports with the N-Force Audit Property reports for the five Property Status Descriptions ("In ATF Custody", "Release Requested", "Release Pending", "Destruction Requested", and "Destruction Pending") that should be included on the financial statements. We identified 94 currency items and 638 firearms that were included in the N-Force Audit Property reports but excluded from the N-Force Query report.

- ATF is not accurately calculating its current-year activity for non-valued firearms (seizures, disposals, and adjustments). We reviewed the Accounting Branch’s methodology for calculating current-year activity and noted that 2,045 items on the N-Force Audit Property reports were not properly reported as current year activity in the financial statement footnote for one of the following reasons:
 - The item was not seized during the current fiscal year, but changed from a status excluded from the footnote to a status included in the footnote during the current fiscal year;
 - The item was both seized and disposed of during the current fiscal year; or
 - The item was included on the FY 2012 N-Force Audit Property report but was not included on the FY 2011 N-Force Audit Property report, even though the “ATF custody date” was prior to FY 2012.

Seized Evidence Bank Account Procedures Need Improvement

We identified discrepancies in ATF’s reconciliation of its Bank of America seized currency account at June 30, 2012. In addition to reviewing the reconciliation, we tested five receipts and five payments recorded in FY 2012. We noted that:

- ATF did not record six checks written on the seized currency bank account in May 2012 to its check register until July. As a result, ATF’s general ledger balance for seized currency was overstated by \$3,802 at June 30.
- ATF’s policy requires that field offices convert seized currency into a cashier’s check and remit the check to Headquarters within five working days to ensure the proper safeguarding of seized currency. However, one field division did not convert \$11,068 from multiple seizures during the period August 2010 through November 2011 to a cashier’s check, and submit it to Headquarters until February 23, 2012.
- ATF recorded an incorrect payee in its check register for one of the payments tested, resulting in an inadequate audit trail for the case.

N-Force Reports Are Not Complete and Accurate

We noted the following issues indicating that the N-Force reports and the N-Force Query reports are not accurate, complete, and reliable:

- During our review of the N-Force Audit Property reports and the N-Force Query reports supporting ATF’s June 30, 2012 financial statement balance and disclosures for seized currency, we identified the following currency items that had incorrect property status information in N-Force. Although the currency items were properly reported on ATF’s financial statements and footnote disclosures, these conditions indicate that N-Force reports are not accurate and complete.
 - Amounts seized for 107 cases had been disposed of prior to June 30, but had a property status of “Release Pending” or “In ATF Custody” in N-Force as of June 30, 2012. ATF attributed most of these discrepancies to actions that the field offices had not taken to update the property status of these items on N-Force.
 - Amounts seized for 13 cases that are currently held in ATF’s Bank of America seized currency account, but were recorded in N-Force with a property status of “Released” or “Destroyed”. The case agents erroneously changed the property status when they submitted the seized amounts to Headquarters.
 - Amounts seized for 216 cases that are currently held in ATF’s Bank of America seized currency account contained a vault status of “Checked Out” or “Disposed”. These amounts should have been “Checked In” to Headquarters N-Force Vault to ensure proper accountability for, and safeguarding of, the seized items.

- We tested a sample of 48 property items from the March 31, 2012, N-Force Query reports. Two of the sample items did not have accurate property status information in N-Force, as follows:
 - One firearm had been destroyed on April 28, 2011, but was categorized in N-Force as “Destruction Pending” as of March 31, 2012, and therefore was still included in the ending non-valued firearms balance. The field office stated that it had prepared a Report of Destruction but could not find the document.
 - One firearm had been transferred to the Martinsburg firearm library in August 2008, but was categorized in N-Force as “Release Requested” as of March 31, 2012 and therefore was still included in the non-valued firearms ending balance. The field office stated that it submitted a Release and Receipt of Property form to the Firearms Technology Branch for signature, but the field office did not receive the signed copy for entry in N-Force.
- During our review of the March 31, 2012 N-Force Audit Property report for vehicles, we identified the following three vehicles that did not have accurate property status information in N-Force. The vehicles were categorized in N-Force as “Destruction Pending” or “Release Pending” as of March 31, 2012 but had been disposed of prior to that date. These vehicles were properly excluded from ATF’s footnote disclosures, but are further evidence that N-Force reports are inaccurate.
 - An Express Van disposed of on January 24, 2008.
 - An Astro Van disposed of on June 19, 2004.
 - A Crown Victoria disposed of on June 19, 2004.

ATF Inventories of Currency and Other Property Seized for Evidence Need Improvement

ATF conducts annual inventories of currency and other property seized for evidence; however, the inventory procedures are not sufficient to ensure that N-Force data is complete, accurate, and reliable. We noted the following:

- ATF’s inventory procedures only include items that are included in N-Force Vault reports, and do not include items that have been checked out of vaults for various reasons, such as checked out to a lab.
- ATF’s inventory procedures are not sufficient to ensure the physical existence and accuracy of N-Force data for vehicles, which are not included in N-Force Vault reports.
- ATF’s inventory procedures do not include a reconciliation between all items included in N-Force reports with property status codes “In ATF Custody”, “Release Requested”, “Release Pending”, “Destruction Requested”, and “Destruction Pending”, which should be reported in the financial statements or footnote disclosures, and those items that are in the N-Force Vault reports.
- ATF only performs an inventory of currency once a year. Best practices would require a more frequent inventory because these items are highly susceptible to loss or misappropriation.
- ATF does not perform a reconciliation or inventory of seized currency deposited into the Bank of America seized currency account (the seized evidence list), amounts held in Headquarters’ vault, and amounts reported in Headquarters’ N-Force Vault report, to ensure that the N-Force reports reflect the appropriate property status and vault status and that all amounts submitted to Headquarters are safeguarded.

ATF’s internal control deficiencies over currency and property seized for evidence may be because ATF does not have documented procedures for identifying and calculating amounts that should be reported and disclosed in the financial statements, and its current processes lack sufficient coordination between the Accounting Branch, AFSPD, the field offices, and OSII. In addition, ATF has not dedicated sufficient resources or provided adequate oversight

to ensure that data in N-Force is updated timely and accurately, and validated to ensure that amounts reported and disclosed for property seized for evidence are complete and accurate.

YEAR-END UNFILLED CUSTOMER ORDER BALANCES

ATF's internal controls to ensure that unfilled customer order balances are accurate as of year-end need improvement. We noted that ATF's September 30, 2012 unfilled customer order balances were overstated by \$14.5 million, due to the following reasons:

- \$13.7 million in single, multi, and no-year reimbursable agreements that are maintained in fund 700R (a single-year fund) for which the unfilled customer order balances were not written off at year-end.
- \$768 thousand in estimated reimbursable payroll and credit card charges recorded on the general ledger as direct expenditures rather than reimbursable expenditures, because the reimbursable project code was not yet identified.

ATF does not have a financial reporting checklist that details all necessary year-end financial-reporting adjustments, and does not perform an analytical procedure to help substantiate the unfilled customer order balances at year-end.

OMB Circular A-123, *Management's Responsibility for Internal Control*, states: "Management is responsible for establishing and maintaining internal control to achieve the objectives of effective and efficient operations, reliable financial reporting, and compliance with applicable laws and regulations."

Statement of Federal Financial Accounting Standards (SFFAS) No. 3, *Accounting for Inventory and Related Property*, Paragraph 61 states that: "Seized monetary instruments shall be recognized as seized assets when seized." Paragraph 62 further states that: "Seized property other than monetary instruments shall be disclosed in the footnotes. The value of the seized property shall be accounted for in an agency's property management records until the property is forfeited, returned, or otherwise liquidated."

SFFAS No. 3, Paragraph 66, requires disclosures that analyze the change in seized property, including the "number of seized property that are (1) on hand at the beginning of the year, (2) made during the year, (3) disposed of during the year, and (4) on hand at the end of the year..."

In accordance with OMB Circular A-11 Section 130.9, performing agencies accounting for reimbursable agreements using an annual Treasury Account Fund Symbol (TAFS) should not show unobligated balances on the September 30, SF 133. However, when the ordering agency's TAFS are multi- or no-year, the performing agency should show the amount of unfilled customer order not obligated as new anticipated spending authority from offsetting collections in its annual TAFS established for the next fiscal year.

RECOMMENDATIONS

We recommend that ATF:

1. Develop documented procedures for identifying and calculating seized amounts to be reported and disclosed in the financial statements. *(New)*

Management Response:

ATF concurs with the audit recommendation and will document and implement procedures for identifying and calculating seized amounts reported and disclosed in the financial statements and notes.

2. Improve supervisory oversight, coordination between ATF offices, and policies and procedures to ensure timely and accurate:
 - recording and reconciliation of seized currency activity;
 - updating of property status and vault status fields in N-Force; and
 - reporting of seized property current-year activity in the financial statement footnotes. *(New)*

Management Response:

ATF concurs with this recommendation and will provide training to address this in FY 2013 to improve the reconciliation of seized cash held in vaults process as well as the accuracy of reporting seized for evidence property in the financial statement footnotes.

3. Revise seized property inventory procedures to ensure that inventories are performed for all property items in N-Force with property status codes "In ATF Custody", "Release Requested", "Release Pending", "Destruction Requested", and "Destruction Pending". *(New)*

Management Response:

ATF concurs with this recommendation and has revised its inventory procedures for FY 2013.

4. Ensure that all field offices are aware of their responsibility to submit seized currency to Headquarters within five days of seizure. *(New)*

Management Response:

ATF concurs with this recommendation and will provide training to the field agents to address this in FY 2013.

ATF's Asset Forfeiture and Seized Property Division (AFSPD) will provide training to address the control deficiencies related to the recording and maintenance of the seized evidence activity in N-FORCE. Training for Special Agents will include the following:

- Processing Seized for Evidence currency;
- Disposal of Seized for Evidence currency;
- Sending currency to AFSPD;
- N-Force entry process; and,
- N-Force Vault process.

A quick reference guide will also be made available to assist in administering seized for evidence items.

5. Update the financial reporting checklist to ensure that all necessary adjustments are recorded at year-end, and implement financial reporting review procedures, such as analytical procedures, to ensure that general ledger accounts have expected balances. *(New)*

Management Response:

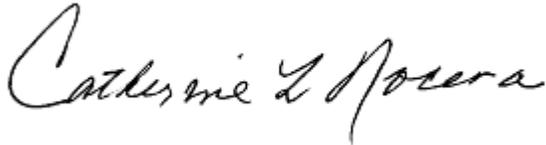
ATF concurs with this recommendation and will address this by implementing a process to include applicable unfiled order accounts and analytical procedures are completed timely and accurately at year-end.

* * * *

We provide the current status of the open recommendations from the prior year in the following Exhibit.

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

COTTON & COMPANY LLP

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Catherine L. Nocera, CPA, CISA
Partner

November 5, 2012
Alexandria, Virginia

STATUS OF PRIOR YEAR'S FINDING AND RECOMMENDATIONS

As required by *Government Auditing Standards* issued by the Comptroller General of the United States, and by OMB Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, as amended, we have reviewed the status of the prior year's finding and recommendations. The following table provides our assessment of the progress ATF has made in correcting the previously identified significant deficiency. We also provide the Office of the Inspector General report number where the deficiency was reported, our recommendation for improvement, and the status of the recommendation as of the end of fiscal year 2012:

Report	Significant Deficiency	Recommendation	Status
Annual Financial Statements Fiscal Year 2011 Report No. 12-14	Controls over Financial Reporting Need Improvement	<p>Recommendation No. 1: ATF needs to establish stronger oversight controls for financial reporting and validation of recorded transactions, including:</p> <ul style="list-style-type: none"> • timely and comprehensive reconciliation of general ledger account balances with subsidiary records; • review and approval of source documentation, calculations, and posting by someone other than the preparer; and • more thorough data analysis and managerial reviews, including performance of more analytical procedures at the transaction, and general ledger account level. 	Completed
		<p>Recommendation No. 2: ATF needs to work with the Department to standardize recording and reporting of upward and downward adjustments.</p>	Completed
		<p>Recommendation No. 3: ATF needs to implement a quality control review process for second-party review of the annual statistical accounts payable accrual rate development, as well as the quarterly accrual calculations.</p>	Completed



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INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND OTHER MATTERS

Inspector General
United States Department of Justice

Acting Director
Bureau of Alcohol, Tobacco, Firearms and Explosives
United States Department of Justice

We have audited the Consolidated Balance Sheets of the Bureau of Alcohol, Tobacco, Firearms and Explosives (ATF), a component of the United States Department of Justice (DOJ), as of September 30, 2012 and 2011, and the related Consolidated Statements of Net Cost, Consolidated Statements of Changes in Net Position, Combined Statements of Budgetary Resources, and Combined Statements of Custodial Activity for the years then ended, and have issued our report thereon dated November 5, 2012. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; 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. 07-04, *Audit Requirements for Federal Financial Statements*, as amended.

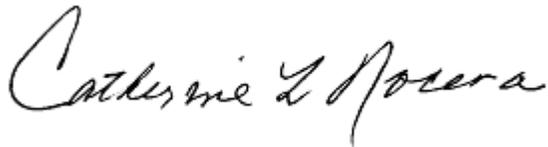
ATF's management is responsible for complying with laws, regulations, and contract agreements applicable to ATF. As part of obtaining reasonable assurance about whether ATF's fiscal year 2012 financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contract agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 07-04, including the provisions referred to in section 803(a) of the *Federal Financial Management Improvement Act of 1996* (FFMIA). 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 tests of compliance, exclusive of those referred to in FFMIA, disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 07-04.

Under FFMIA, we are required to report whether ATF's financial management systems substantially comply with federal financial management system requirements, applicable federal accounting standards, and application of the United States 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 tests of FFMIA disclosed no instances in which ATF's financial management systems did not substantially comply with the requirements described in the preceding paragraph.

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

COTTON & COMPANY LLP

A handwritten signature in black ink that reads "Catherine L. Nocera". The signature is written in a cursive, flowing style.

Catherine L. Nocera, CPA, CISA
Partner

November 5, 2012
Alexandria, Virginia

**Principal Financial Statements
and Related Notes**

See Independent Auditors' Report on Financial Statements

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U.S. Department of Justice
Bureau of Alcohol, Tobacco, Firearms and Explosives
Consolidated Balance Sheets
As of September 30, 2012 and 2011

Dollars in Thousands	2012	2011
ASSETS (Note 2)		
Intragovernmental		
Fund Balance with U.S. Treasury (Note 3)	\$ 232,563	\$ 241,768
Accounts Receivable, Net (Note 5)	37,105	27,803
Other Assets (Note 8)	1,514	7,643
Total Intragovernmental	<u>271,182</u>	<u>277,214</u>
Cash and Monetary Assets (Note 4)	71,196	68,184
Accounts Receivable, Net (Note 5)	352	256
General Property, Plant and Equipment, Net (Note 7)	206,737	210,262
Advances and Prepayments	963	786
Total Assets	<u>\$ 550,430</u>	<u>\$ 556,702</u>
LIABILITIES (Note 9)		
Intragovernmental		
Accounts Payable	\$ 13,996	\$ 14,942
Accrued Federal Employees' Compensation Act Liabilities	20,852	20,074
Other Liabilities (Note 12)	10,450	10,474
Total Intragovernmental	<u>45,298</u>	<u>45,490</u>
Accounts Payable	42,947	45,450
Actuarial Federal Employees' Compensation Act Liabilities	116,959	110,697
Accrued Payroll and Benefits	33,917	34,276
Accrued Annual and Compensatory Leave Liabilities	51,019	51,897
Seized Cash and Monetary Instruments (Notes 4 and 11)	4,932	3,527
Capital Lease Liabilities (Note 10)	394	1,071
Other Liabilities (Note 12)	61,073	59,905
Total Liabilities	<u>\$ 356,539</u>	<u>\$ 352,313</u>
NET POSITION		
Unexpended Appropriations - All Other Funds	\$ 175,104	\$ 174,210
Cumulative Results of Operations - All Other Funds	18,787	30,179
Total Net Position	<u>\$ 193,891</u>	<u>\$ 204,389</u>
Total Liabilities and Net Position	<u>\$ 550,430</u>	<u>\$ 556,702</u>

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

U.S. Department of Justice
Bureau of Alcohol, Tobacco, Firearms and Explosives
Consolidated Statements of Net Cost
For the Fiscal Years Ended September 30, 2012 and 2011

Dollars in Thousands

	FY	Gross Costs			Less: Earned Revenues			Net Cost of Operations (Note 14)
		Intra-governmental	With the Public	Total	Intra-governmental	With the Public	Total	
Goal 1	2012	\$ -	\$ 6,419	\$ 6,419	\$ -	\$ -	\$ -	\$ 6,419
	2011	\$ -	\$ 5,649	\$ 5,649	\$ -	\$ -	\$ -	\$ 5,649
Goal 2	2012	383,250	895,426	1,278,676	80,866	503	81,369	1,197,307
	2011	381,239	886,810	1,268,049	90,650	650	91,300	1,176,749
Total	2012	<u>\$ 383,250</u>	<u>\$ 901,845</u>	<u>\$ 1,285,095</u>	<u>\$ 80,866</u>	<u>\$ 503</u>	<u>\$ 81,369</u>	<u>\$ 1,203,726</u>
	2011	<u>\$ 381,239</u>	<u>\$ 892,459</u>	<u>\$ 1,273,698</u>	<u>\$ 90,650</u>	<u>\$ 650</u>	<u>\$ 91,300</u>	<u>\$ 1,182,398</u>

Goal 1 Prevent Terrorism and Promote the Nation's Security Consistent with the Rule of Law

Goal 2 Prevent Crime, Protect the Rights of the American People, and Enforce Federal Law

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

U.S. Department of Justice
Bureau of Alcohol, Tobacco, Firearms and Explosives
Consolidated Statements of Changes in Net Position
For the Fiscal Years Ended September 30, 2012 and 2011

Dollars in Thousands	2012	2011
Unexpended Appropriations		
Beginning Balances	\$ 174,210	\$ 202,183
Budgetary Financing Sources		
Appropriations Received	1,152,000	1,114,772
Appropriations Transferred-In/Out	(15,067)	(7,892)
Other Adjustments	-	(2,231)
Appropriations Used	(1,136,039)	(1,132,622)
Total Budgetary Financing Sources	894	(27,973)
Unexpended Appropriations	\$ 175,104	\$ 174,210
Cumulative Results of Operations		
Beginning Balances	\$ 30,179	\$ 29,258
Budgetary Financing Sources		
Appropriations Used	1,136,039	1,132,622
Other Financing Sources		
Transfers-In/Out Without Reimbursement	15,949	3,153
Imputed Financing from Costs Absorbed by Others (Note 15)	40,346	47,544
Total Financing Sources	1,192,334	1,183,319
Net Cost of Operations	(1,203,726)	(1,182,398)
Net Change	(11,392)	921
Cumulative Results of Operations	\$ 18,787	\$ 30,179
Net Position	\$ 193,891	\$ 204,389

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

U.S. Department of Justice
Bureau of Alcohol, Tobacco, Firearms and Explosives
Combined Statements of Budgetary Resources
For the Fiscal Years Ended September 30, 2012 and 2011

Dollars in Thousands	2012	2011
Budgetary Resources		
Unobligated Balance, Brought Forward, October 1	\$ 60,967	\$ 110,131
Recoveries of Prior Year Unpaid Obligations	32,746	21,159
Other Changes in Unobligated Balance	(14,933)	(7,780)
Unobligated Balance from Prior Year Budget Authority, Net	<u>78,780</u>	<u>123,510</u>
Appropriations	1,151,866	1,112,429
Spending Authority from Offsetting Collections	<u>94,820</u>	<u>85,420</u>
Total Budgetary Resources	<u>\$ 1,325,466</u>	<u>\$ 1,321,359</u>
Status of Budgetary Resources		
Obligations Incurred (Note 16)	\$ 1,279,257	\$ 1,260,392
Unobligated Balance, End of Period:		
Apportioned	29,929	38,931
Unapportioned	<u>16,280</u>	<u>22,036</u>
Total Unobligated Balance - End of Period	<u>46,209</u>	<u>60,967</u>
Total Status of Budgetary Resources:	<u>\$ 1,325,466</u>	<u>\$ 1,321,359</u>
Change in Obligated Balance		
Obligated Balance, Net - Brought Forward, October 1		
Unpaid Obligations, Gross	\$ 245,431	\$ 226,042
Less: Uncollected Customer Payments from Federal Sources	<u>59,852</u>	<u>70,397</u>
Total Obligated Balance, Net - Brought Forward, October 1	185,579	155,645
Obligations Incurred	1,279,257	1,260,392
Less: Outlays, Gross	1,233,314	1,219,844
Change in Uncollected Customer Payments from Federal Sources	(7,219)	10,545
Less: Recoveries of Prior Year Unpaid Obligations	32,746	21,159
Obligated Balance, Net - End of Period		
Unpaid Obligations, Gross	\$ 258,628	245,431
Less: Uncollected Customer Payments from Federal Sources	<u>67,071</u>	<u>59,852</u>
Total Obligated Balance, Net - End of Period	<u>\$ 191,557</u>	<u>\$ 185,579</u>
Budgetary Authority and Outlays, Net:		
Budgetary Authority, Gross	\$ 1,246,686	\$ 1,197,849
Less: Actual Offsetting Collections	87,601	95,965
Change in Uncollected Customer Payments from Federal Sources	(7,219)	10,545
Budget Authority, Net	<u>\$ 1,151,866</u>	<u>\$ 1,112,429</u>
Outlays, Gross	\$ 1,233,314	\$ 1,219,844
Less: Actual Offsetting Collections	87,601	95,965
Outlays, Net	<u>1,145,713</u>	<u>1,123,879</u>
Less: Distributed Offsetting Receipts	2,859	3,892
Agency Outlays, Net	<u>\$ 1,142,854</u>	<u>\$ 1,119,987</u>

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

U.S. Department of Justice
Bureau of Alcohol, Tobacco, Firearms and Explosives
Combined Statements of Custodial Activity
For the Fiscal Years Ended September 30, 2012 and 2011

Dollars in Thousands	2012	2011
Revenue Activity		
Sources of Cash Collections		
Fees and Licenses	\$ 21,710	\$ 17,437
Fines, Penalties and Restitution Payments - Civil	18	20
Fines, Penalties and Restitution Payments - Criminal	74	95
Miscellaneous	2,873	3,892
Total Cash Collections	24,675	21,444
Accrual Adjustments	13	26
Total Custodial Revenue	24,688	21,470
Disposition of Collections		
Transferred to Federal Agencies		
U.S. Department of the Treasury	(24,328)	(21,138)
Refunds and Other Payments	(360)	(332)
Net Custodial Activity (Note 17)	<u>\$ -</u>	<u>\$ -</u>

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

Notes to the Financial Statements
(Dollars in Thousands, Except as Noted)

1. Summary of Significant Accounting Policies

A. Reporting Entity

The Bureau of Alcohol, Tobacco, Firearms and Explosives (ATF or the Bureau), a principal law enforcement agency, is within the Department of Justice (DOJ or the Department). ATF's mission is to reduce violent crime, prevent terrorism, and promote the Nation's security. The men and women of ATF perform the dual responsibilities of enforcing Federal criminal laws and regulating the firearms and explosive industries.

B. Basis of Presentation

These financial statements have been prepared from the books and records of ATF in accordance with United States generally accepted accounting principles issued by the Federal Accounting Standards Advisory Board (FASAB) and presentation guidelines in the Office of Management and Budget (OMB) Circular A-136, *Financial Reporting Requirements*. These financial statements are different from the financial reports prepared pursuant to OMB directives which are used to monitor and control the use of ATF's budgetary resources.

Throughout these financial statements, intragovernmental assets, liabilities, earned revenues, and costs have been classified according to the type of entity with which the transactions are made. Intragovernmental assets and liabilities are those from or to other Federal entities. Intragovernmental earned revenues are collections or accruals of revenue from other Federal entities and intragovernmental costs are payments or accruals of payments to other Federal entities.

To ensure that ATF's financial statements are meaningful at the entity level and to enhance reporting consistency within the Department, Other Assets and Other Liabilities as defined by OMB Circular A-136 have been disaggregated on the balance sheet. These include Advances and Prepayments, Accrued Federal Employees' Compensation Act Liabilities, Accrued Payroll and Benefits, Accrued Annual and Compensatory Leave Liabilities, Seized Cash and Monetary Instruments, Capital Lease Liabilities, and Contingent Liabilities.

These notes are an integral part of these financial statements.

1. Summary of Significant Accounting Policies (continued)

C. Basis of Consolidation

The consolidated/combined financial statements include the accounts of ATF. All significant proprietary intra-entity transactions and balances have been eliminated in consolidation. The Statements of Budgetary Resources and Statements of Custodial Activity are combined statements for FYs 2012 and 2011, and as such, intra-entity transactions have not been eliminated.

D. Basis of Accounting

Transactions are recorded on the accrual and budgetary basis of accounting. Under the accrual basis, revenues are recorded when earned and expenses are recorded when incurred, regardless of when cash is exchanged. Under the budgetary basis, however, funds availability is recorded based upon legal considerations and constraints. As a result, certain line items on the proprietary financial statements may not equal similar line items on the budgetary financial statements. The Combined Statements of Custodial Activity are presented on a modified cash basis. Civil and criminal debt collections are recorded when the Department receives payment from debtors to the Federal Government. Accrual adjustments are made related to collections of fees and licenses.

E. Non-Entity Assets

Non-entity assets are those assets that are held by ATF but are not available for use by ATF. Non-entity assets are reported on ATF's Consolidated Balance Sheets as accounts receivable, and cash and monetary assets. Non-entity accounts receivable consists of taxpayer debts due to ATF. Non-entity assets equal non-entity liabilities. Non-entity assets are not considered a financing source (revenue) available to offset operating expenses of ATF.

F. Fund Balance with U.S. Treasury and Cash

The Department of the Treasury (Treasury) processes the Bureau's cash receipts and disbursements. Entity fund balance with Treasury and cash are primarily appropriated funds available to pay current liabilities and to finance authorized purchase commitments.

ATF does not have disbursing authority. ATF maintains cash in commercial banks to facilitate the replenishment of the Bureau's imprest funds as well as seized cash held for evidence, and special operations.

These notes are an integral part of these financial statements.

1. Summary of Significant Accounting Policies (continued)

G. Accounts Receivable, Net

Intragovernmental accounts receivable consist of amounts due under reimbursable agreements with Federal entities for services provided by ATF. Accounts receivable due from Federal agencies are considered to be fully collectible. Public accounts receivable consists of employee and vendor accounts receivable. An allowance for doubtful accounts is established for public accounts receivable when it is more likely than not that the accounts receivable will not be collected. The allowance is based on the debtor's ability to pay, debtor's payment record, and probability of recovery.

H. General Property, Plant and Equipment

Personal property and equipment purchased with a cost greater than or equal to \$25,000 (dollars) per unit and a useful life of two years or more, is capitalized and depreciated. Other equipment is expensed when purchased. Real property and leasehold improvements with a cost greater than or equal to \$100,000 (dollars) per unit, and a useful life of two years or more, is capitalized and depreciated. Leasehold improvements are amortized over the lesser of the life of the lease or useful life of the asset. Normal repairs and maintenance are charged to expense as incurred.

ATF also capitalizes internal use software when costs are greater than or equal to \$500,000 (dollars). The same threshold also applies to enhancements that add significant functionality to the software. ATF amortizes business software over seven years and personal productivity software over three years. Depreciation and amortization are calculated using the straight-line method.

As a Bureau under Treasury, ATF's policy was to capitalize bulk purchases that are defined as purchases of multiple similar items that on an individual basis do not meet the capitalization threshold, but when purchased as a lot, exceeded \$250,000 (dollars). This policy was consistent with Treasury's policy. The Department does not have a similar policy; therefore, beginning January 24, 2003 (the date of transfer to DOJ), such bulk purchases are no longer capitalized. Due to the large dollar amount of capitalized bulk purchases, ATF has been allowed to let them depreciate over time versus writing them off all at once. ATF has approximately \$6 (net) of bulk purchases remaining in General Property, Plant and Equipment as of September 30, 2012, which will be fully depreciated by the end of FY 2013.

These notes are an integral part of these financial statements.

1. Summary of Significant Accounting Policies (continued)

I. Advances and Prepayments

Prepayments are payments made to individuals or other organizations to cover certain periodic expenses before those expenses are incurred. In accordance with Public Law 91-614, ATF participates in the Treasury's Working Capital Fund from which it receives services on a reimbursable basis. Payments made in advance are authorized for services that have been deemed more advantageous and economical when provided centrally. Advances and prepayments involving other Federal agencies are classified as Other Assets on the Balance Sheet.

ATF prepaid to the General Services Administration (GSA) \$28,441 in costs related to the construction of its new headquarters building. Those prepaid costs were considered construction in progress and land acquisition when they occurred. ATF does not hold title to the land. The building was substantially complete in FY 2007 and the prepaid costs were transferred out of construction in progress and land, and recognized as a prepayment. The prepaid costs have been expensed over five years in accordance with rent credits specified in the GSA occupancy agreement. As of September 30, 2012, the prepaid costs are fully expensed.

J. Forfeited and Seized Property

ATF seizes property in consequence of a violation of public law. Generally, seized property includes monetary instruments, various types of weapons, ammunition and explosives. Seized property can be held for evidence, forfeited, or destroyed. All property seized for evidence is maintained by ATF. This property is recorded at the estimated fair market value at the time of the seizure and is not adjusted for any subsequent increases and decreases in estimated fair value. ATF discloses the value of personal property when the individual item seized is worth \$1,000 (dollars) or more at the time of seizure. Seized cash is recorded as an asset under Cash and Monetary Assets. The offsetting liability is recorded under Seized Cash and Monetary Instruments.

ATF also participates in the DOJ Assets Forfeiture Fund (the Fund). ATF is reimbursed by the Fund for carrying out forfeiture activities. ATF contributes forfeited property to the Fund. Firearms that are seized for forfeiture are either returned, destroyed, or placed into official use. Non-prohibited property includes property such as real estate, vehicles, cash, Title I Firearms (as defined in Title 18 USC Section 922(a) (3)), ammunition and other personal property that is in itself legal to possess. Title 18 USC 3051 and the regulations therein, prohibit the sale of firearms or the transfer of firearms owned by the United States to anyone other than another Federal government entity. ATF's seized prohibited property (contraband) may include illegal drugs and untaxed liquor. All other types of property are legal to possess, however, the possessor may be prohibited from possession.

These notes are an integral part of these financial statements.

1. Summary of Significant Accounting Policies (continued)

J. Forfeited and Seized Property (continued)

Quantities of illegal drugs and firearms held as evidence are disclosed in Note 6 in accordance with Statement of Federal Financial Accounting Standards (SFFAS) No. 3, *Accounting for Inventory and Related Property*, and Federal Financial Accounting and Auditing Technical Release No. 4, *Reporting on Non-Valued Seized and Forfeited Property*. Reported quantities of drugs include only substances over one kilogram (KG) that are laboratory-analyzed and confirmed.

K. Liabilities

Liabilities represent the amount of monies, or other resources, that are likely to be paid by ATF as the result of a transaction or event. However, no liability can be paid by ATF without an appropriation. Liabilities for which an appropriation has not been enacted, and for which there is uncertainty an appropriation will be enacted, are classified as liabilities not covered by budgetary resources. Also, liabilities of ATF arising from other than contracts can be abrogated by the Government acting in its sovereign capacity.

Intragovernmental liabilities consist of amounts payable to the Treasury for custodial fees collected by ATF, payables to other Federal agencies, and accrued Federal Employees' Compensation Act (FECA) charges. In addition, public liabilities are amounts due to be refunded to taxpayers and other payables due to public vendors.

Other Liabilities consists primarily of project-generated proceeds. The proceeds will be transferred to the Department of the Treasury General Fund at the conclusion of the project.

L. Contingencies and Commitments

ATF is party to various administrative proceedings, legal actions, and claims. The balance sheet includes an estimated liability for those legal actions where management and the Chief Counsel consider adverse decisions “probable” and amounts are reasonably estimable. Legal actions where management and the Chief Counsel consider adverse decisions “probable” or “reasonably possible” and the amounts are reasonably estimable are disclosed in Note 13, Contingencies and Commitments. However, there are cases where amounts have not been accrued or disclosed because the amounts of the potential loss cannot be estimated or the likelihood of an unfavorable outcome is considered “remote.”

These notes are an integral part of these financial statements.

1. Summary of Significant Accounting Policies (continued)

M. Annual, Sick, and Other Leave

Annual and compensatory leave earned by ATF employees, but not yet used, is reported as an accrued liability. Annual leave is accrued as it is earned by employees and is included in personnel compensation and benefit costs. An unfunded liability is recognized for earned but unused annual leave since from a budgetary standpoint, this annual leave will be paid from future appropriations when the leave is used by employees rather than from amounts that were appropriated to ATF as of the date of the financial statements. The amount accrued is based upon current pay rates of the employees. Sick leave and other types of leave are expensed when used and no liability is recognized for these amounts, as employees do not vest in these benefits.

N. Interest on Late Payments

Pursuant to the Prompt Payment Act, 31 U.S.C. § 3901-3907, Federal agencies must pay interest on payments for goods or services made to business concerns after the due date. The due date is generally 30 days after receipt of a proper invoice or acceptance of the goods or services, whichever is later.

O. Retirement Plans

With few exceptions, employees hired before January 1, 1984, are covered by the Civil Service Retirement System (CSRS) and employees hired after December 31, 1983, are covered by the Federal Employees Retirement System (FERS).

For employees covered by the CSRS, ATF contributes 7 percent of the employee's gross pay for normal retirement or 7.5 percent for law enforcement retirement. For employees covered by the FERS, ATF contributes 11.9 percent of the employee's gross pay for normal retirement or 26.3 percent for law enforcement retirement. All employees are eligible to contribute to the Federal Thrift Savings Plan (TSP). For those employees covered by the FERS, a TSP is automatically established, and ATF is required to contribute an additional 1 percent of gross pay to this plan and match employee contributions up to 4 percent. No matching contributions are made to the TSPs established by the CSRS employees. ATF does not report CSRS or FERS assets, accumulated plan benefits, or unfunded liabilities, if any, which may be applicable to its employees. Such reporting is the responsibility of the Office of Personnel Management (OPM).

These notes are an integral part of these financial statements.

1. Summary of Significant Accounting Policies (continued)

O. Retirement Plans (continued)

SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, requires employing agencies to recognize the cost of pensions and other retirement benefits during their employees' active years of service. Refer to Note 15, Imputed Financing from Costs Absorbed by Others.

P. Federal Employee Compensation Benefits

FECA provides income and medical cost protection to covered Federal civilian employees injured on the job and employees who have incurred a work-related injury or occupational disease. The future workers' compensation estimates were generated from an application of actuarial procedures developed to estimate the liability for FECA benefits. The actuarial liability estimates for FECA benefits include the expected liability for death, disability, medical and miscellaneous costs for approved compensation cases. The liability is determined using the paid losses extrapolation method, which is calculated over the next 37-year period. This method utilizes historical benefit payment patterns related to a specific incurred period to predict ultimate payments related to that period. The projected annual benefit payments were discounted to present value.

Claims are paid for ATF employees by the Department of Labor (DOL) from the FECA fund, for which ATF reimburses DOL. The accrued liability represents claims paid by DOL for ATF employees, for which the fund has not been reimbursed. The actuarial liability is an estimate of future costs to be paid on claims made by ATF employees. The estimated future cost is not obligated against budgetary resources until the year in which the cost is billed to ATF.

Q. Intragovernmental Activity

Intragovernmental costs and exchange revenue represent transactions made between two reporting entities within the Federal government. Costs and earned revenues with the public represent exchange transactions made between the reporting entity and a non-Federal entity. The classification of revenue or cost as "intragovernmental" or "with the public" is defined on a transaction-by-transaction basis. The purpose of this classification is to enable the Federal government to prepare consolidated financial statements, not to match public and intragovernmental revenue with the costs incurred to produce public and intragovernmental revenue.

These notes are an integral part of these financial statements.

1. Summary of Significant Accounting Policies (continued)

R. Revenues and Other Financing Sources

(1) Exchange Revenues

Exchange revenues are inflows of resources to a government entity that the entity has earned by providing something of value to the public or another government entity at a price. ATF, currently, has agreements in place which are reimbursed through the Department of Justice Assets Forfeiture Fund. In addition, ATF provides a number of services including law enforcement, training and professional development, and science and information technology to other government agencies through reimbursable agreements. Exchange revenues are presented on the Consolidated Statements of Net Cost. ATF's exchange revenues from other government agencies include an agreement with the U.S. Department of State to train explosives-detecting canines for foreign countries. The canines are used in foreign countries to combat terrorism and protect American travelers abroad. Similarly, ATF is funded on a reimbursable basis for activity related to enforcement of the Controlled Substances Act.

(2) Nonexchange Revenues

Nonexchange revenues are inflows of resources that the government demands or receives by donation. For ATF, most nonexchange revenues result from collecting fees from firearms and explosives industries. As ATF is unable to keep any of these collections, they are recognized as custodial revenue and a corresponding liability when collected.

Nonexchange revenues are presented on the Combined Statements of Custodial Activity as all amounts are transferred to the Treasury General Fund.

(3) Other Financing Sources

Other financing sources provide inflows of resources during the reporting period and include appropriations used and financing imputed with respect to any cost subsidies. Unexpended appropriations are recognized separately in determining net position but are not financing sources until used.

ATF receives the majority of the funding needed to support its operations through congressional appropriations. The appropriations received are

These notes are an integral part of these financial statements.

1. Summary of Significant Accounting Policies (continued)

(3) Other Financing Sources (continued)

annual, multi-year, and no-year funding that may be used, within statutory limits, for operating and capital expenditures (primarily equipment, furniture, and furnishings). Appropriations are also received to meet specific program objectives. The Bureau's activities are funded by the following:

- 15120700 – *Salaries and Expenses Appropriation and Reimbursable Authority*
- 15X0700 – *No-year Salaries and Expenses and Spectrum Relocation Fund*
- 15X0720 – *No-year Appropriation for Construction Funding*
- 1511/120700 – *Two-year Appropriation for High Intensity Drug Trafficking Area Initiative*
- 1512/130700 – *Two-year Appropriation for High Intensity Drug Trafficking Area Initiative*
- 15X8526 – *Microstamping*

The above appropriations and the related gross costs, revenues, and the net costs as shown in the Consolidated Statements of Net Cost are in Federal budget functional classification 750, Administration of Justice. The accompanying financial statements include the accounts of the above six Treasury symbols as well as eleven expired Treasury Symbols which are under ATF control.

Appropriations are recognized as a financing source at the time the related program or administrative expenditure is incurred. Costs financed by other Federal entities on behalf of ATF are recognized as imputed financing sources as required by SFFAS No. 5.

Other financing sources also include non-financial distributions, such as seized property, received by ATF from the DOJ Assets Forfeiture Fund. These resources are used in law enforcement initiatives.

S. Earmarked Funds

SFFAS No. 27 defines 'earmarked funds' as being financed by specifically identified revenues, often supplemented by other financing sources, which remain

These notes are an integral part of these financial statements.

1. Summary of Significant Accounting Policies (continued)

S. Earmarked Funds (continued)

available over time. These specifically identified revenues and other financing sources are required by statute to be used for designated activities, benefits, or purposes, and must be accounted for separately from the Government's general revenues. The three required criteria for an earmarked fund are:

1. A statute committing the Federal Government to use specifically identified revenues and other financing sources only for designated activities, benefits, or purposes;
2. Explicit authority for the earmarked fund to retain revenues and other financing sources not used in the current period for future use to finance the designated activities, benefits, or purposes; and
3. A requirement to account for and report on the receipt, use, and retention of the revenues and other financing sources that distinguishes the earmarked fund from the Government's general revenues.

ATF does not have any funds that meet the definition of an earmarked fund.

T. Tax Exempt Status

As an agency of the Federal Government, ATF is exempt from all income taxes imposed by any governing body whether it be a Federal, state, commonwealth, local, or foreign government.

U. Use of Estimates

The preparation of financial statements requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

V. Reclassifications

The FY 2011 financial statements were reclassified to conform to the FY 2012 Departmental financial statement presentation requirements. Changes to the presentation of the Combined and Combining Statements of Budgetary Resources were made, in accordance with guidance provided in OMB Circular A-136, "*Financial Reporting Requirements*" and as such, activity and balances reported on the FY 2011 Combined and Combining Statement of Budgetary Resources

These notes are an integral part of these financial statements.

1. Summary of Significant Accounting Policies (continued)

V. Reclassifications (continued)

other prior year amounts have also been reclassified to conform with the current year presentation. The reclassifications had no material effect on total assets, liabilities, net position, change in net position or budgetary resources as previously reported.

W. Subsequent Events

Subsequent events and transactions occurring after September 30, 2012 through the date of the auditors' opinion have been evaluated for potential recognition or disclosure in the financial statements. The date of the auditors' opinion also represents the date that the financial statements were available to be issued.

2. Non-Entity Assets

Non-entity assets are assets that are held by ATF but are not available for use by ATF. Non-entity assets are primarily project-generated proceeds and seized cash.

As of September 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
With the Public		
Cash and Monetary Assets	\$ 65,993	\$ 63,406
Total Entity Assets	<u>484,437</u>	<u>493,296</u>
Total Assets	<u>\$ 550,430</u>	<u>\$ 556,702</u>

These notes are an integral part of these financial statements.

3. Fund Balance with U.S. Treasury

As of September 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Fund Balance		
Trust Funds	\$ 1,029	\$ 1,029
General Funds	<u>231,534</u>	<u>240,739</u>
Total Fund Balance with U.S. Treasury	<u>\$ 232,563</u>	<u>\$ 241,768</u>
Status of Fund Balances		
Unobligated Balance - Available	\$ 29,929	\$ 38,931
Unobligated Balance - Unavailable	16,280	22,036
Obligated Balance not yet Disbursed	191,557	185,579
Other Funds (With)/Without Budgetary Resources	<u>(5,203)</u>	<u>(4,778)</u>
Total Status of Fund Balance	<u>\$ 232,563</u>	<u>\$ 241,768</u>

As of September 30, 2012 and 2011, Other Funds (With)/Without Budgetary Resources consisted of amounts held in ATF agent cashier (imprest) funds.

4. Cash and Monetary Assets

As of September 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Cash		
Imprest Funds	\$ 5,203	\$ 4,778
Other Cash	<u>61,061</u>	<u>59,879</u>
	<u>66,264</u>	<u>64,657</u>
Monetary Assets		
Seized Monetary Instruments	<u>4,932</u>	<u>3,527</u>
Total Cash and Monetary Assets	<u>\$ 71,196</u>	<u>\$ 68,184</u>

Cash available for ATF use represents agent cashier (imprest) funds. The agent cashier funds are used to finance the purchase of evidence and information from informants in open ATF investigations and enforcement operations. Other Cash consists of project – generated proceeds from undercover operations.

5. Accounts Receivable, Net

As of September 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Intragovernmental		
Accounts Receivable	\$ 37,105	\$ 27,803
With the Public		
Accounts Receivable	442	315
Allowance for Uncollectible Accounts	<u>(90)</u>	<u>(59)</u>
Total With the Public	<u>352</u>	<u>256</u>
Total Accounts Receivable	<u>\$ 37,457</u>	<u>\$ 28,059</u>

Intragovernmental accounts receivable consist of amounts due under reimbursable agreements with Federal entities for services provided by ATF. Accounts receivable due from Federal agencies are considered to be fully collectible. Public accounts receivable consist of employee and vendor accounts receivables.

These notes are an integral part of these financial statements.

6. Seized Property

Property is seized during the course of an investigation. This property is considered contraband, evidence of a crime, or subject to forfeiture. All seized for forfeiture property is reported by the DOJ Assets Forfeiture Fund. The seized for evidence personal property category includes computers, vehicles, and other miscellaneous items. Other seized property includes monetary instruments, handguns, machine guns, rifles and shotguns. Seized property that will be destroyed, such as firearms, is reported as the number of items seized, and is not considered to have a value.

Seized Monetary Instruments were valued at \$4,932 as of September 30, 2012, and \$3,527 as of September 30, 2011. Seized Monetary Instruments is recorded as an asset under Cash and Monetary Assets along with the offsetting liability under Seized Cash and Monetary Instruments.

6. Seized Property (continued)

For the Fiscal Year Ended September 30, 2012

Seized Property Category		Beginning Balance	Adjust- ments	Seizures	Disposals	Ending Balance
Seized for Evidence						
Seized Monetary						
Instruments	Value	\$ 3,527	\$ -	\$ 4,718	\$ 3,313	\$ 4,932
Personal Property *	Number	42	12	10	28	36
	Value	\$ 290	\$ 333	\$ 105	\$ 198	\$ 530
Non-Valued						
Firearms **	Number	29,906	1,078	11,595	11,145	31,434

* Adjustments for personal property are items seized prior to FY 2012 that were not previously recorded.

**Adjustments for non-valued firearms include property action status changes for firearms that were seized in a prior year and items seized prior to FY 2012 that were not previously recorded.

For the Fiscal Year Ended September 30, 2011

Seized Property Category		Beginning Balance	Adjust- ments	Seizures	Disposals	Ending Balance
Seized for Evidence						
Seized Cash Deposited and Seized Monetary						
Instruments	Value	\$ 3,010	\$ -	\$ 6,789	\$ 6,272	\$ 3,527
Personal Property *	Number	177	(105)	6	36	42
	Value	\$ 1,725	\$ (977)	\$ 38	\$ 496	\$ 290
Non-Valued						
Firearms **	Number	13,445	7,307	10,150	996	29,906

* Adjustments for personal property are items classified as seized administratively and seized judicially that were determined to be seized for forfeiture. In prior years, these items were included in the seized for evidence balance.

**Adjustments for non-valued firearms are items classified as abandoned or purchased. In prior years, these items were not included in the seized for evidence balance.

These notes are an integral part of these financial statements.

6. Seized Property (continued)

Method of Disposition of Seized Property:

During FY 2012 and 2011, \$198 and \$496 of valued property seized for evidence were returned to parties with a bonafide interest, and \$3,313 and \$6,272 were either released to a designated party or transferred to the appropriate federal entity under forfeiture or abandonment proceedings. Non-valued property was primarily disposed of through destruction.

7. General Property, Plant and Equipment, Net

As of September 30, 2012	Acquisition Cost	Accumulated Depreciation	Net Book Value	Useful Life
Land and Land Rights	\$ 3,200	\$ -	\$ 3,200	N/A
Improvements to Land	4,926	(1,187)	3,739	15 yrs
Construction in Progress	507	-	507	N/A
Buildings, Improvements, and Renovations	137,255	(26,643)	110,612	40 yrs
Structures	183	(4)	179	20 yrs
Vehicles	48,613	(32,215)	16,398	3-6 yrs
Equipment	83,087	(67,308)	15,779	3-10 yrs
Assets Under Capital Lease	2,235	(1,552)	683	5-6 yrs
Leasehold Improvements	118,327	(79,741)	38,586	2-20 yrs
Internal Use Software	19,003	(13,149)	5,854	3-7 yrs
Internal Use Software in Development	11,200	-	11,200	N/A
Total	\$ 428,536	\$ (221,799)	\$ 206,737	
As of September 30, 2011	Acquisition Cost	Accumulated Depreciation	Net Book Value	Useful Life
Land and Land Rights	\$ 3,200	\$ -	\$ 3,200	N/A
Improvements to Land	4,584	(866)	3,718	15 yrs
Construction in Progress	2,216	-	2,216	N/A
Buildings, Improvements, and Renovations	137,018	(23,566)	113,452	40 yrs
Vehicles	42,586	(29,410)	13,176	3-6 yrs
Equipment	84,161	(71,761)	12,400	3-10 yrs
Assets Under Capital Lease	3,497	(1,916)	1,581	5-6 yrs
Leasehold Improvements	120,026	(75,412)	44,614	2-20 yrs
Internal Use Software	19,003	(11,240)	7,763	3-7 yrs
Internal Use Software in Development	8,142	-	8,142	N/A
Total	\$ 424,433	\$ (214,171)	\$ 210,262	

These notes are an integral part of these financial statements.

7. General Property, Plant and Equipment, Net (continued)

Capitalized Property Purchases from Federal/the Public

	<u>2012</u>	<u>2011</u>
Capitalized Property Purchases from Federal		
Construction in Progress	\$ 319	\$ 1,727
Improvements to Land	92	-
Buildings, Improvements, and Renovations	(36)	3,739
Structures	137	-
Vehicles	2,619	848
Equipment	-	(768)
Leasehold Improvements	123	3,866
Total purchased from Federal Sources	<u>\$ 3,254</u>	<u>\$ 9,412</u>
Capitalized Property Purchases from the Public		
Construction in Progress	\$ (7)	\$ (244)
Buildings, Improvements, and Renovations	74	133
Vehicles	4,398	1,983
Equipment	8,154	7,998
Leasehold Improvements	974	2,161
Internal Use Software	3,058	5,234
Total purchased from the Public	<u>16,651</u>	<u>17,265</u>
Total Capitalized Purchases	<u>\$ 19,905</u>	<u>\$ 26,677</u>

These amounts include current year adjustments in the property accounts.

ATF owns land located in Ammendale, Maryland that is recorded at its acquisition value. There are no restrictions on the use or convertibility of property and equipment.

These notes are an integral part of these financial statements.

8. Other Assets

As of September 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Intragovernmental		
Advances and Prepayments	\$ 1,502	\$ 7,615
Other Intragovernmental Assets	<u>12</u>	<u>28</u>
Total Other Assets	<u>\$ 1,514</u>	<u>\$ 7,643</u>

As of September 30, 2012, prepayments consisted of \$1,427 to the Treasury Working Capital Fund (WCF), and \$75 to Office of Justice Programs (OJP). The remaining \$12 was due to ATF from the Treasury General Fund. As of September 30, 2011, prepayments consisted of \$5,688 to General Services Administration (GSA), \$1,715 to WCF, \$149 to OJP, and \$63 to Department of Defense. The remaining \$28 was due to ATF from the Treasury General Fund.

These notes are an integral part of these financial statements.

9. Liabilities not Covered by Budgetary Resources

As of September 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Intragovernmental		
Accrued FECA Liabilities	\$ 20,852	\$ 20,074
Other Unfunded Employment Related Liabilities	<u>36</u>	<u>51</u>
Total Intragovernmental	<u>20,888</u>	<u>20,125</u>
With the Public		
Actuarial FECA Liabilities	116,959	110,697
Accrued Annual and Compensatory Leave Liabilities	<u>51,019</u>	<u>51,897</u>
Total With the Public	<u>167,978</u>	<u>162,594</u>
Total Liabilities not Covered by Budgetary Resources	188,866	182,719
Total Liabilities Covered by Budgetary Resources	<u>167,673</u>	<u>169,594</u>
Total Liabilities	<u>\$ 356,539</u>	<u>\$ 352,313</u>

Generally, liabilities not covered by budgetary resources are liabilities for which Congressional action is needed before budgetary resources can be provided.

10. Leases

As of September 30, 2012 and 2011

Capital Leases	<u>2012</u>	<u>2011</u>
Summary of Assets Under Capital Lease		
Machinery and Equipment	\$ 2,235	\$ 3,497
Accumulated Depreciation	<u>(1,552)</u>	<u>(1,916)</u>
Total Assets Under Capital Lease (Note 7)	<u>\$ 683</u>	<u>\$ 1,581</u>

Future Capital Lease Payments Due

	<u>Machinery and Equipment</u>
<u>Fiscal Year</u>	
2013	<u>\$ 556</u>
Total Future Capital Lease Payments	\$ 556
Less: Imputed Interest	(5)
Less: Executory Costs	<u>(157)</u>
FY 2012 Net Capital Lease Liabilities	<u>\$ 394</u>
FY 2011 Net Capital Lease Liabilities	<u>\$ 1,071</u>

	<u>2012</u>	<u>2011</u>
Net Capital Lease Liabilities Covered by Budgetary Resources	\$ 394	\$ 1,071

ATF has one capital lease comprised of 257 postage meters along with associated equipment. The total capital asset value is \$2,235 with accumulated depreciation of \$1,552. As of September 30, 2012 capital lease liability for machinery and equipment was \$394. The postal equipment, with the exception of the meters, is leased to own. The meters remain the property of the United States Postal Service. The postal meter lease amortizes through FY 2013.

These notes are an integral part of these financial statements.

10. Leases (continued)

As of September 30, 2012

Future Noncancelable Operating Lease Payments

<u>Fiscal Year</u>	<u>Buildings</u>
2013	\$ 3,015
2014	3,037
2015	3,060
2016	3,061
2017	2,432
After 2017	<u>2,428</u>
Total Future Noncancelable Operating Lease Payments	<u>\$ 17,033</u>

These notes are an integral part of these financial statements.

11. Seized Cash and Monetary Instruments

ATF's seized monetary instruments were \$4,932 as of September 30, 2012, and \$3,527 as of September 30, 2011. All of this cash is seized in the course of law enforcement activities and is held as evidence pending the outcome of any criminal proceedings.

12. Other Liabilities

As of September 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Intragovernmental		
Employer Contributions and Payroll Taxes Payable	\$ 10,366	\$ 10,315
Other Post-Employment Benefits Due and Payable	48	108
Other Unfunded Employment Related Liabilities	<u>36</u>	<u>51</u>
Total Intragovernmental	<u>10,450</u>	<u>10,474</u>
With the Public		
Other Accrued Liabilities	12	26
Other Liabilities	<u>61,061</u>	<u>59,879</u>
Total with the Public	<u>61,073</u>	<u>59,905</u>
Total Other Liabilities	<u>\$ 71,523</u>	<u>\$ 70,379</u>

All Other Liabilities are considered current. Other Liabilities with the public, primarily consists of project-generated proceeds. The proceeds will be remitted to the Treasury General Fund at the conclusion of the project.

These notes are an integral part of these financial statements.

13. Contingencies and Commitments

	<u>Accrued Liabilities</u>	<u>Estimated Range of Loss</u>	
		<u>Lower</u>	<u>Upper</u>
As of September 30, 2012			
Probable	\$ -	\$ -	\$ -
Reasonably Possible		6,001	7,500
As of September 30, 2011			
Probable	\$ -	\$ -	\$ -
Reasonably Possible		6,000	7,500

These notes are an integral part of these financial statements.

14. Net Cost of Operations by Suborganization

For the Fiscal Year Ended September 30, 2012

	<u>Suborganizations</u>			
	Firearms	Explosives and Arson	Alcohol and Tobacco	Consolidated
Goal 1: Prevent Terrorism and Promote the Nation's Security Consistent with the Rule of Law				
Cost of Operations	\$ -	\$ 6,419	\$ -	\$ 6,419
Goal 2: Prevent Crime, Protect the Rights of the American People, and Enforce Federal Law				
Gross Cost	992,464	263,645	22,567	1,278,676
Less: Earned Revenue	60,624	19,625	1,120	81,369
Net Cost of Operations	<u>931,840</u>	<u>244,020</u>	<u>21,447</u>	<u>1,197,307</u>
Net Cost of Operations	<u>\$ 931,840</u>	<u>\$ 250,439</u>	<u>\$ 21,447</u>	<u>\$ 1,203,726</u>

These notes are an integral part of these financial statements.

14. Net Cost of Operations by Suborganization (continued)

For the Fiscal Year Ended September 30, 2011

	<u>Suborganizations</u>			
	Firearms	Explosives and Arson	Alcohol and Tobacco	Consolidated
Goal 1: Prevent Terrorism and Promote the Nation's Security Consistent with the Rule of Law				
Cost of Operations	\$ 2,319	\$ 3,269	\$ 61	\$ 5,649
Goal 2: Prevent Crime, Protect the Rights of the American People, and Enforce Federal Law				
Gross Cost	958,955	284,639	24,455	1,268,049
Less: Earned Revenue	68,502	21,374	1,424	91,300
Net Cost of Operations	890,453	263,265	23,031	1,176,749
Net Cost of Operations	<u>\$ 892,772</u>	<u>\$ 266,534</u>	<u>\$ 23,092</u>	<u>\$ 1,182,398</u>

ATF activity primarily supports DOJ's goal to Prevent Crime, Protect the Rights of the American People, and Enforce Federal Law. ATF participation in the Joint Terrorism Task Force and the Terrorist Device Analysis Center supports DOJ's goal to Prevent Terrorism and Promote the Nation's Security Consistent with the Rule of Law. Revenue is not associated with this goal.

15. Imputed Financing from Costs Absorbed by Others

Imputed Inter-Departmental Financing Sources are the unreimbursed (i.e., non-reimbursed and under-reimbursed) portion of the full costs of goods and services received by ATF from a providing entity that is not part of the U.S. Department of Justice. In accordance with SFFAS No. 30, *Inter-Entity Cost Implementation Amending SFFAS 4, Managerial Cost Accounting Standards and Concepts*, the material Imputed Inter-Departmental financing sources recognized by ATF are the cost of benefits for the Federal Employees Health Benefits Program (FEHB), the Federal Employees' Group Life Insurance Program (FEGLI), the Federal pension plans that are paid by other Federal entities, and any un-reimbursed payments made from the Treasury Judgment Fund on behalf of ATF. The Treasury Judgment Fund was established by the Congress and funded at 31 U.S.C. 1304 to pay in whole or in part the court judgments and settlement agreements negotiated by the Department on behalf of agencies, as well as certain types of administrative awards. Interpretation of Federal Financial Accounting Standards Interpretation No. 2, *Accounting for Treasury Judgment Fund Transactions*, requires agencies to recognize liabilities and expenses when unfavorable litigation outcomes are probable and the amount can be estimated and will be paid by the Treasury Judgment Fund.

SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, requires that employing agencies recognize the cost of pensions and other retirement benefits during their employees' active years of service. SFFAS No. 5 requires OPM to provide cost factors necessary to calculate cost. OPM actuaries calculate the value of pension benefits expected to be paid in the future, and then determine the total funds to be contributed by and for covered employees, such that the amount calculated would be sufficient to fund the projected pension benefits. For employees covered by Civil Service Retirement System (CSRS), the cost factors are 29.8% of basic pay for regular, 50.9% law enforcement officers, 23.2% regular offset, and 45.2% law enforcement officers offset. For employees covered by Federal Employees Retirement System (FERS), the cost factors are 13.7% of basic pay for regular and 29.7% for law enforcement officers.

The cost to be paid by other agencies is the total calculated future costs, less employee and employer contributions. In addition, the cost of other retirement benefits, which include health and life insurance that are paid by other Federal entities, must also be recorded.

Imputed Intra-Departmental Financing Sources as defined in SFFAS No. 4, *Managerial Cost Accounting Concepts and Standards for the Federal Government*, are the unreimbursed portion of the full costs of goods and services received by ATF from a providing entity that is part of the U.S. Department of Justice. Recognition is required for those transactions determined to be material to the receiving entity. The determination of whether the cost is material requires considerable judgment based on the specific facts and circumstances of each type of good or service provided. ATF does not have any imputed Intra-Departmental financing sources. SFFAS No. 4 also states that

These notes are an integral part of these financial statements.

15. Imputed Financing from Costs Absorbed by Others (continued)

costs for broad and general support need not be recognized by the receiving entity, unless such services form a vital and integral part of the operations or output of the receiving entity. Costs are considered broad and general if they are provided to many, if not all, reporting components and not specifically related to the receiving entity's output. Those costs determined to be material are presented in the table below.

For the Fiscal Years Ended September 30, 2012 and 2011

	2012	2011
Imputed Inter-Departmental Financing		
Treasury Judgment Fund	\$ 785	\$ 1,214
Health Insurance	24,961	27,099
Life Insurance	106	109
Pension	14,494	19,122
Total Imputed Inter-Departmental	\$ 40,346	\$ 47,544

Judgment Fund payments for FY 2012 and FY 2011 were paid by the Treasury on behalf of ATF.

ATF does not report CSRS assets, FERS assets, accumulated plan benefits or unfunded liabilities, if any, applicable to retirement plans because the accounting for and reporting of such amounts is the responsibility of OPM. Based on cost factors provided by OPM, estimated future pension benefits for ATF employees, to be paid by OPM as of September 30, 2012 and September 30, 2011, are included in the chart above. Similarly, OPM, rather than ATF, reports liabilities for future payments to retired employees who participate in the FEHB and the FEGLI Program. The FY 2012 and FY 2011 FEHB cost factors applied to a weighted average number of employees enrolled in the FEHB were \$5,817 (dollars) and \$6,027 (dollars), respectively. The FEGLI cost factor for employees enrolled in the FEGLI program, as provided by OPM, was .02 percent of their basic pay.

16. Information Related to the Statement of Budgetary Resources

Apportionment Categories of Obligations Incurred:

The amount of direct and reimbursable obligations against amounts apportioned under Category A and B are reported in the table below. The apportionment categories are determined in accordance with the guidance provided in Part 4 of OMB Circular A-11, *Preparation, Submission and Execution of the Budget*. Category A represents resources apportioned for calendar quarters. Category B represents resources apportioned for other time periods; for activities, projects, and objectives or for a combination thereof.

	<u>Direct Obligations</u>	<u>Reimbursable Obligations</u>	<u>Total Obligations Incurred</u>
For the Fiscal Year Ended September 30, 2012			
Obligations Apportioned Under			
Category A	\$ 1,161,241	\$ 108,180	\$1,269,421
Category B	9,836	-	9,836
Total	<u>\$1,171,077</u>	<u>\$ 108,180</u>	<u>\$1,279,257</u>
For the Fiscal Year Ended September 30, 2011			
Obligations Apportioned Under			
Category A	\$ 1,125,706	\$ 86,110	\$1,211,816
Category B	48,576	-	48,576
Total	<u>\$1,174,282</u>	<u>\$ 86,110</u>	<u>\$1,260,392</u>

These notes are an integral part of these financial statements.

16. Information Related to the Statement of Budgetary Resources (continued)

Status of Undelivered Orders:

Undelivered orders (UDO) represent the amount of goods and/or services ordered, which have not been actually or constructively received. This amount includes any orders which may have been prepaid or advanced but for which delivery or performance has not yet occurred.

As of September 30, 2012 and 2011

	2012	2011
UDO Obligations Unpaid	\$ 156,962	\$ 139,274
UDO Obligations Prepaid/Advanced	2,465	8,401
Total UDO	\$ 159,427	\$ 147,675

Legal Arrangements Affecting Use of Unobligated Balances:

Unobligated balances represent the cumulative amount of budget authority that is not obligated and that remains available for obligation based on annual legislative requirements and other enabling authorities, unless otherwise restricted. The use of unobligated balances is restricted based on annual legislation requirements and other enabling authorities. Funds are appropriated on an annual, multi-year, and no-year basis. Appropriated funds shall expire on the last day of availability and are no longer available for new obligations. Unobligated balances in unexpired fund symbols are available in the next fiscal year for new obligations unless some restrictions had been placed on those funds by law. Amounts in expired fund symbols are not available for new obligations, but may be used to adjust previously established obligations.

16. Information Related to the Statement of Budgetary Resources (continued)

Statement of Budgetary Resources vs. the Budget of the United States Government:

The reconciliation as of September 30, 2012 is not presented because the submission of the Budget of the United States Government (Budget) for FY 2014, which presents the execution of the FY 2012 Budget, occurs after publication of these financial statements. The Department of Justice Budget Appendix can be found on the OMB website (<http://www.whitehouse.gov/omb/budget>) and will be available in early February 2013.

For the Fiscal Year Ended September 30, 2011

(Dollars in millions)

	<u>Budgetary Resources</u>	<u>Obligations Incurred</u>	<u>Distributed Offsetting Receipts</u>	<u>Net Outlays</u>
Statement of Budgetary Resources (SBR)	\$ 1,321	\$ 1,260	\$ 4	\$ 1,120
Funds not Reported in the Budget				
Expired Funds	(31)	(7)		
Reconciling Item	1	(2)		
Distributed Offsetting Receipts			(4)	4
Budget of the United States Government	<u>\$ 1,291</u>	<u>\$ 1,251</u>	<u>\$ -</u>	<u>\$ 1,124</u>

These notes are an integral part of these financial statements.

17. Net Custodial Revenue Activity

As an agent of the Federal government and as authorized by 26 U.S.C. § 6301, ATF collects fees from firearms and explosives industries, as well as import, permit and license fees. In addition, Special Occupation Taxes are collected from certain firearms businesses. Also, miscellaneous collections include project-generated proceeds. As ATF is unable to use these collections in its operations, ATF is required to transfer these collections to the Treasury General Fund. The ATF custodial collections totaled \$24,675 and \$21,444 for the fiscal years ended September 30, 2012 and 2011, respectively.

These collections represent the balances in the Combined Statements of Custodial Activity. These authorities are granted under the Gun Control Act, Title XI of the Organized Crime Control Act of 1970, and the Safe Explosives Act. All authorities granted by these laws were transferred from the Treasury to DOJ under the Homeland Security Act of 2002.

All of the fees collected by ATF net of related refund disbursements are remitted to the Treasury General Fund. The Treasury further distributes this revenue to Federal agencies in accordance with various laws and regulations. There were no custodial liabilities as of September 30, 2011 and 2012.

18. Reconciliation of Net Cost of Operations (proprietary) to Budget (formerly the Statement of Financing)

For the Fiscal Years Ended September 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Resources Used to Finance Activities		
Budgetary Resources Obligated		
Obligations Incurred	\$ 1,279,257	\$ 1,260,392
Less: Spending Authority from Offsetting Collections and Recoveries	<u>127,566</u>	<u>106,579</u>
Obligations Net of Offsetting Collections and Recoveries	1,151,691	1,153,813
Less: Offsetting Receipts	<u>2,859</u>	<u>3,892</u>
Net Obligations	1,148,832	1,149,921
Other Resources		
Transfers-In/Out Without Reimbursement	15,949	3,153
Imputed Financing from Costs Absorbed by Others (Note 15)	<u>40,346</u>	<u>47,544</u>
Net Other Resources Used to Finance Activities	<u>56,295</u>	<u>50,697</u>
Total Resources Used to Finance Activities	1,205,127	1,200,618
Resources Used to Finance Items not Part of the Net Cost of Operations		
Net Change in Budgetary Resources Obligated for Goods, Services, and Benefits Ordered but not Yet Provided	(13,834)	(17,138)
Resources That Fund Expenses Recognized in Prior Periods (Note 19)	(893)	(4,074)
Budgetary Offsetting Collections and Receipts That do not Affect Net Cost of Operations	2,859	3,892
Resources That Finance the Acquisition of Assets	<u>(19,905)</u>	<u>(26,677)</u>
Total Resources Used to Finance Items not Part of the Net Cost of Operations	<u>(31,773)</u>	<u>(43,997)</u>
Total Resources Used to Finance the Net Cost of Operations	\$ 1,173,354	\$ 1,156,621

These notes are an integral part of these financial statements.

18. Reconciliation of Net Cost of Operations (proprietary) to Budget (formerly the Statement of Financing) (continued)

For the Fiscal Years Ended September 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Components of Net Cost of Operations That Will not Require or Generate Resources in the Current Period		
Components That Will Require or Generate Resources in Future Periods (Note 19)	\$ 6,944	\$ 4,117
Depreciation and Amortization	23,210	23,918
Revaluation of Assets or Liabilities	218	(2,258)
Total Components of Net Cost of Operations That Will not Require or Generate Resources in the Current Period	<u>30,372</u>	<u>25,777</u>
Net Cost of Operations	<u>\$ 1,203,726</u>	<u>\$ 1,182,398</u>

These notes are an integral part of these financial statements.

19. Explanation of Differences Between Liabilities not Covered by Budgetary Resources and Components of Net Cost of Operations Requiring or Generating Resources in Future Periods

Liabilities that are not covered by realized budgetary resources and for which there is no certainty that budgetary authority will be realized, such as the enactment of an appropriation, are considered liabilities not covered by budgetary resources. These liabilities totaling \$188,866 and \$182,719 on September 30, 2012 and 2011, respectively, are discussed in Note 9, Liabilities not Covered by Budgetary Resources. Decreases in these liabilities result from current year budgetary resources that were used to fund expenses recognized in prior periods. Increases in these liabilities represent unfunded expenses that were recognized in the current period. These increases along with the change in the portion of exchange revenue receivables from the public, which are not considered budgetary resources until collected, represent components of current period net cost of operations that will require or generate budgetary resources in future periods. The changes in liabilities not covered by budgetary resources and receivables generating resources in future periods are comprised of the following:

For the Fiscal Years Ended September 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Resources that Fund Expenses Recognized in Prior Periods		
Decrease in Accrued Annual and Compensatory Leave Liabilities	\$ (878)	\$ (511)
Other		
Decrease in Contingent Liabilities	-	(3,505)
Decrease in Other Unfunded Employment Related Liabilities	(15)	-
Decrease in Other Post Employment Benefits Due and Payable	-	(58)
Total Other	<u>(15)</u>	<u>(3,563)</u>
Total Resources that Fund Expenses Recognized in Prior Periods	<u>\$ (893)</u>	<u>\$ (4,074)</u>
Components of Net Cost of Operations That Will Require or Generate Resources in Future Periods		
(Increase)/Decrease in Receivable from the Public	(96)	(94)
Other		
Increase in Actuarial FECA Liabilities	6,262	3,685
Increase in Accrued FECA Liabilities	778	507
Increase in Other Unfunded Employment Related Liabilities	-	19
Total Other	<u>7,040</u>	<u>4,211</u>
Total Components of Net Cost of Operations That Will Require or Generate Resources in Future Periods	<u>\$ 6,944</u>	<u>\$ 4,117</u>

These notes are an integral part of these financial statements.

Required Supplementary Information

Unaudited

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U.S. Department of Justice
Bureau of Alcohol, Tobacco, Firearms and Explosives
Required Supplementary Information
Combining Statements of Budgetary Resources
Unaudited

For the Fiscal Year Ended September 30, 2012

For the Fiscal Year Ended September 30, 2011

Dollars in Thousands	2012			2011		
Budgetary Resources	Appropriated	Trust Funds	Cumulative	Appropriated	Trust Funds	Cumulative
Unobligated Balance, Brought Forward, October 1	\$ 59,938	\$ 1,029	\$ 60,967	\$ 109,102	\$ 1,029	\$ 110,131
Recoveries of Prior Year Unpaid Obligations	32,746	-	32,746	21,159	-	21,159
Other Changes in Unobligated Balance	(14,933)	-	(14,933)	(7,780)	-	(7,780)
Unobligated Balance from Prior Year Budget Authority, Net	77,751	1,029	78,780	122,481	1,029	123,510
Appropriations	1,151,866	-	1,151,866	1,112,429	-	1,112,429
Spending Authority from Offsetting Collections	94,820	-	94,820	85,420	-	85,420
Total Budgetary Resources	\$ 1,324,437	\$ 1,029	\$ 1,325,466	\$ 1,320,330	\$ 1,029	\$ 1,321,359
Status of Budgetary Resources						
Obligations Incurred	\$ 1,279,257	\$ -	\$ 1,279,257	\$ 1,260,392	\$ -	\$ 1,260,392
Unobligated Balance - End of Period						
Apportioned	29,929	-	29,929	38,931	-	38,931
Unapportioned	15,251	1,029	16,280	21,007	1,029	22,036
Total Unobligated Balance - End of Period	45,180	1,029	46,209	59,938	1,029	60,967
Total Status of Budgetary Resources	\$ 1,324,437	\$ 1,029	\$ 1,325,466	\$ 1,320,330	\$ 1,029	\$ 1,321,359
Change in Obligated Balance						
Obligated Balance, Net - Brought Forward, October 1						
Unpaid Obligations, Gross	\$ 245,431	\$ -	\$ 245,431	\$ 226,042	\$ -	\$ 226,042
Less: Uncollected Customer Payments from Federal Sources	59,852	-	59,852	70,397	-	70,397
Total Obligated Balance, Net - Brought Forward, October 1	185,579	-	185,579	155,645	-	155,645
Obligations Incurred	1,279,257	-	1,279,257	1,259,363	1,029	1,260,392
Less: Gross Outlays	1,233,314	-	1,233,314	1,219,844	-	1,219,844
Change in Uncollected Customer Payments from Federal Sources	(7,219)	-	(7,219)	10,545	-	10,545
Less: Recoveries of Prior Year Unpaid Obligations	32,746	-	32,746	21,159	-	21,159
Obligated Balance, Net - End of Period						
Unpaid Obligations	258,628	-	258,628	245,431	-	245,431
Less: Uncollected Customer Payments from Federal Sources	67,071	-	67,071	59,852	-	59,852
Total Obligated Balance, Net - End of Period	\$ 191,557	\$ -	\$ 191,557	\$ 185,579	\$ -	\$ 185,579
Budgetary Authority and Outlays, Net:						
Budgetary Authority, Gross	\$ 1,246,686	\$ -	\$ 1,246,686	\$ 1,197,849	\$ -	\$ 1,197,849
Less: Actual Offsetting Collections	87,601	-	87,601	95,965	-	95,965
Change in Uncollected Customer Payments from Federal Sources	(7,219)	-	(7,219)	10,545	-	10,545
Budget Authority, Net	\$ 1,151,866	\$ -	\$ 1,151,866	\$ 1,112,429	\$ -	\$ 1,112,429
Outlays, Gross	\$ 1,233,314	\$ -	\$ 1,233,314	\$ 1,219,844	\$ -	\$ 1,219,844
Less: Actual Offsetting Collections	87,601	-	87,601	95,965	-	95,965
Outlays, Net	1,145,713	-	1,145,713	1,123,879	-	1,123,879
Less: Distributed Offsetting Receipts	2,859	-	2,859	3,892	-	3,892
Agency Outlays, Net	\$ 1,142,854	\$ -	\$ 1,142,854	\$ 1,119,987	\$ -	\$ 1,119,987

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Other Accompanying Information

Unaudited

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U.S. Department of Justice
Bureau of Alcohol, Tobacco, Firearms and Explosives
Combined Schedule of Spending
For the Fiscal Year Ended September 30, 2012
Unaudited

Dollars in Thousands

Total Amounts Agreed to be Spent

Total Resources	\$ 1,325,466
Less: Amount Available but Not Agreed to be Spent	29,929
Less: Amount Not Available to be Spent	16,280
Total Amounts Agreed to be Spent	\$ 1,279,257

How was the Money Spent?

Personnel Compensation and Benefits

11xx	Personnel Compensation	\$ 539,938
12xx	Personnel Benefits	220,419
13xx	Benefits of Former Personnel	4,209
21xx	Travel & Transportation of Persons	25,261
22xx	Transportation of Things	2,760

Other Program Related Expenses

23xx	Rent	119,649
24xx	Printing and Reproduction	1,002
25xx	Other Services	257,027
26xx	Supplies and Materials	24,308
31xx	Equipment/IT Software	34,862
32xx	Leasehold Improvements	3,466
42xx	Insurance Claims and Indemnities	413

Total Spending	1,233,314
Amounts Remaining to be Spent	45,943
Total Amounts Agreed to be Spent	\$ 1,279,257

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Appendix

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OFFICE OF THE INSPECTOR GENERAL ANALYSIS AND SUMMARY OF ACTIONS NECESSARY TO CLOSE THE REPORT

The Office of the Inspector General (OIG) provided a draft of the *Independent Auditors' Report on Internal Control over Financial Reporting* to the Bureau of Alcohol, Tobacco, Firearms and Explosives (ATF). ATF's response is incorporated in the *Independent Auditors' Report on Internal Control over Financial Reporting* of this final report. The following provides the OIG analysis of the response and summary of actions necessary to close the report.

Recommendation Number:

- 1. Resolved.** ATF concurred with our recommendation. This recommendation can be closed when subsequent annual financial statement audit testing verifies that ATF has developed documented procedures for identifying and calculating seized amounts to be reported and disclosed in the financial statements.
- 2. Resolved.** ATF concurred with our recommendation. This recommendation can be closed when subsequent annual financial statement audit testing verifies that ATF has improved supervisory oversight, coordination between ATF offices, and policies and procedures to ensure timely and accurate recording and reconciliation of seized currency activity; updating of property status and vault status fields in N-Force; and reporting of seized property current-year activity in the financial statement footnotes.
- 3. Resolved.** ATF concurred with our recommendation. This recommendation can be closed when subsequent annual financial statement audit testing verifies that ATF has revised seized property inventory procedures to ensure that inventories are performed for all property items in N-Force with property status codes "In ATF Custody", "Release Requested", "Release Pending", "Destruction Requested", and "Destruction Pending".
- 4. Resolved.** ATF concurred with our recommendation. This recommendation can be closed when subsequent annual financial statement audit testing verifies that ATF has ensured that all field offices are aware of their responsibility to submit seized currency to Headquarters within 5 days of seizure.

5. **Resolved.** ATF concurred with our recommendation. This recommendation can be closed when subsequent annual financial statement audit testing verifies that ATF has updated the financial reporting checklist to ensure that all necessary adjustments are recorded at year-end, and implemented financial reporting review procedures, such as analytical procedures, to ensure that general ledger accounts have expected balances.