California Prison Industry Authority
REPORT TO THE LEGISLATURE
Fiscal Year 2013-14

QUALITY PRODUCTS
CHANGED LIVES
A SAFER CALIFORNIA

CALPIA
Quality Products ★ Changed Lives ★ A Safer California

Edmund G. Brown Jr.
Governor
State of California

California Prison Industry Board

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The Prison Industry Board (PIB) Fiscal Year 2013-14 Report to the Legislature regarding the California Prison Industry Authority (CALPIA) is submitted pursuant to Chapter 1549, Statutes of 1982, as embodied in paragraph 2808 (k) of the California Penal Code which requires the PIB to report to the Legislature in writing on or before February 1, of each year regarding the following:

1. The financial activity and condition of each enterprise under its jurisdiction.
2. The plans of the board regarding any significant changes in existing operations.
3. The plans of the board regarding the development of new enterprises.
4. A breakdown, by institution, of the number of prisoners at each institution, working in enterprises under the jurisdiction of the CALPIA.

Committed to California's Public Safety

The Prison Industry Board

The Prison Industry Board (PIB) was established in 1983, (Pursuant to Chapter 1549, Statutes of 1982) to oversee the California Prison Industry Authority. The same legislation reconstituted the former California Correctional Industries Commission as CALPIA.

The PIB oversees CALPIA operations, much like a corporate board of directors. The PIB sets general policy for CALPIA, oversees the performance of existing CALPIA industries, determines which new industries shall be established, and appoints and monitors the performance of CALPIA's CEO/General Manager. The PIB also serves as a public hearing body, ensuring that both CALPIA enterprises are self-sufficient and that they do not have a substantial adverse effect upon the private sector. The PIB actively solicits public input for the decisions it makes to expand existing or develop new prison industries.

The Penal Code[1] Established CALPIA to:

- Develop and operate manufacturing, agricultural and service enterprises that provide work opportunities for incarcerated offenders under the jurisdiction of the California Department of Corrections and Rehabilitation (CDCR) and serve government agencies with products and services commensurate with their needs.

- Create and maintain working conditions within the enterprises as much like those which prevail in private industry as possible, to assure offenders employed therein the opportunity to work productively, to earn funds, and to acquire or improve effective work habits and occupational skills.

- Operate work programs for offenders that are self-supporting through the generation of sufficient funds from the sale of products and services to pay all its expenses, thereby avoiding the cost of alternative inmate programming by CDCR. CALPIA receives no annual appropriation from the Legislature.

CALPIA Mission Statement

CALPIA is a self-supporting, customer-focused business that provides productive work and skill development opportunities to offenders to reduce recidivism, increase public safety and prison safety.

CALPIA Program Goal

CALPIA's program goal is to produce trained offenders that have a job skill, good work habits, basic education and job support in the community when they parole so they never return to prison. CALPIA offenders receive industry accredited certifications that employers require. CALPIA offender programming reduces prison violence and makes communities safer by lowering the frequency of repeat criminal behavior.

Does CALPIA Work?

Over a three year period, beginning in Fiscal Year (FY) 2007-2008, CALPIA participants returned to prison, on average, 26 to 38 percent less often than offenders released from the CDCR general population, saving the General Fund millions in incarceration costs. Additionally, offenders who participate in CALPIA's Career Technical Education (CTE) program are 91 percent less likely to return to prison.

Does CALPIA Save the State Money?

CALPIA's offender programming saves the State General Fund millions annually through lower recidivism and saves CDCR millions more by providing rehabilitation programs that CDCR does not have to fund.

To achieve its mission, CALPIA has established five main strategic and business goals:

- Achieve Self-Sufficiency
- Build Offender Success
- Exceed Customer Expectations
- Ensure an Effective and Well-Trained Workforce
- Promote and Support CALPIA

1. Penal Code Section 2800-2818

Correctional Industries

CALPIA manages 90 manufacturing, service and consumable factories. As of January 2015, CALPIA's operations are in 28 CDCR institutions and by November 1, 2015, CALPIA will be at all 34 CDCR institutions compared to FY 2013-14 in which CALPIA was operating at 25 institutions. CALPIA provides employment and programming for approximately 8,000 offenders assigned to 6,800 positions annually in manufacturing, consumable service, and support functions including warehouse and administration. The CALPIA Administrative offices are located in Folsom, California.

The goods and services produced by CALPIA's enterprises are sold predominately to departments of the State of California, as well as other government entities. CDCR is CALPIA's largest customer and accounted for 57.12 percent of all sales in FY 2013-2014, down from 57.4 percent in FY 2012-2013, and 57.6 percent in FY 2011-2012. Other major State customers include the Department of Motor Vehicles (DMV), the Department of State Hospitals (DSH), the Department of Transportation (Caltrans), the Department of General Services (DGS), the Department of Forestry and Fire Protection (CAL FIRE), the Department of Military, the Department of Veteran Affairs (CDVA), the California Highway Patrol (CHP), California Correctional Health Care Services (CCHCS), and the Board of Equalization (BOE).

Joint and Free Venture Programs

On behalf of CDCR, CALPIA manages California's Joint Venture Program (JVP), which is responsible for implementing the Prison Inmate Labor Initiative, Proposition 139 of 1990. Under its provisions, private businesses may establish business operations inside California correctional facilities and hire offenders. This includes only those businesses that are starting a new company, expanding an existing business, or relocating to California.

CALPIA also manages the Free Venture Program (FVP), which operates in much the same way as the JVP, except it is located within California's State juvenile facilities.

Offenders are paid a comparable wage that is then subject to deductions for room and board, crime victim compensation, prisoner family support, government ordered restitution and mandatory offender savings for post-release. In addition, offender-employees pay federal and state taxes. The JVP disbursed more than $130,000 for crime victim restitution in FY 2013-14. As of October 2012, local government correctional facilities may also participate in the JVP.

Career Technical Education

The CALPIA Career Technical Education (CTE) program[2], was established in 2006. The program began as a pre-apprenticeship program with instruction being administered by journeyman instructors under contract from local trade unions representing Carpentry, Construction Labor and Iron Working. Program graduates, upon parole are able to obtain employment in their specific apprenticeship with trade tools provided by CALPIA. The program also includes Marine Technology (Deep Sea Diving), Facilities Maintenance and in 2014, CALPIA added a technology component to their CTE portfolio with Computer-Aided Design (CAD) and Computer Coding. In 2015, 75 percent of the CALPIA CTE participants will be female offenders. The CALPIA CTE program is currently funded via contractual agreement with the CDCR Division of Rehabilitation Programs and the Governor's 2015-2016 Budget Bill includes $2.6 million to continue the contractual arrangement.

2. Under Penal Code Section 2805, CALPIA may initiate and develop new vocational training programs as well as assume jurisdiction over existing vocational training programs.

To date, the CALPIA CTE program has been one of the most effective rehabilitation programs in California. In 2012, the Prison Industry Board approved an assessment report of the CALPIA CTE program from FYs 2007-08 through 2010-11. The report shows that cumulatively, CALPIA CTE graduates have a recidivism rate of 7.13 percent. Although there may be other relevant factors that contribute to lowering recidivism, CALPIA participants are significantly more likely to become productive citizens that pay taxes instead of costing California taxpayers by returning to prison. The full study is available at www.calpia.ca.gov.

The CALPIA CTE program is divided into seven areas:

1. Carpentry
2. Iron Working
3. Construction Labor
4. Commercial Diving
5. Facilities Maintenance
6. AutoCAD (Computer-Aided Design)
7. Computer Coding

Industry Employment Program

CALPIA developed the Industry Employment Program (IEP) to enhance the ability of offender workers to obtain meaningful jobs upon release and successfully transition from prison to the community and the workforce. This effort supports CALPIA's goal to reduce recidivism and contribute to safer communities.

Through the IEP, CALPIA offender workers are continually evaluated for improvement in job skills, education, experience and work habits. The IEP provides offender workers access to nationally accredited certifications and internal skill proficiency certificates.

All CALPIA offender participants must achieve a General Education Development (GED) degree within two years to continue participating in CALPIA programs.

The IEP provides transition to employment services and information. An appointment at the DMV is arranged to provide valid identification, within a week after parole. Information and forms are provided for a social security card, birth certificate, child support and veteran's benefits. The IEP also provides access to the CDCR statewide resource guide for paroling offenders.

CALPIA prepares offenders for productive lives and reduces incarceration costs

Paroled offenders who participated in CALPIA programs are less likely to return to prison than those who did not participate in CALPIA.

The recidivism rate of CALPIA participants is an essential measure of the organization's success. Over a three-year period, beginning in FY 2007-08, CALPIA participants returned to prison, on average, 26 to 38 percent less often than offenders released from the CDCR general population, saving the General Fund millions in incarceration costs. Additionally, offenders who participate in CALPIA's CTE program are 91 percent less likely to return to prison.

CALPIA provides CDCR over 6,000 offender programming positions annually, thereby saving CDCR more than $11 million annually in General Fund costs for rehabilitation positions that CDCR does not have to fund.[3]

3. Legislative Analyst's Office (2011) Rehabilitation Programs (http://www.lao.ca.gov/laoapp/LAOMenus/Sections/crim_justice/6_cj_inmatecost.aspx?catid=3)

Future Measurement of Recidivism

Previously, the rate of recidivism for CALPIA offenders was based solely on an offender's physical custody return to a CDCR institution after violating parole or committing a new criminal offense and comparing that rate of return to that of CDCR offenders who did not participate in CALPIA programs. Post implementation of AB 109 (2011 Public Safety Realignment), there is a greater potential for a former CDCR offender who reoffends to then be held in the custody of a county jail rather than eventually return to a CDCR institution.

Previous to 2015, CALPIA was unable to collect recidivism data that would accurately document if a former CALPIA offender was returned to custody at the county level. Beginning in 2015, CALPIA will begin collecting recidivism data of CALPIA participants at both the state and local levels utilizing an independent government partner for data collection. This measurement will provide CALPIA and the public the most accurate evaluation of the rate of recidivism of both traditional CALPIA correctional industry programs, but also the highly successful CALPIA CTE programs.

Fiscal Year	Total CALPIA Parolees	Total CDCR Parolees	1 Year			2 Years			3 Years		
			CALPIA Percent	CDCR Percent	Variance Percent	CALPIA Percent	CDCR Percent	Variance Percent	CALPIA Percent	CDCR Percent	Variance Percent
10/11*	1,402		20.40%								
09/10*	1,364	105,598	23.61%	45.70%	48.34%	33.65%					
08/09*	1,471	112,934	27.46%	45.20%	39.25%	38.55%	56.90%	32.25%	42.96%		
07/08	1,549	116,063	31.18%	47.50%	34.36%	42.09%	59.20%	28.90%	46.80%	63.70%	26.53%
06/07	1,693	115,254	30.89%	47.90%	35.51%	43.89%	60.50%	27.45%	48.32%	65.10%	25.78%
05/06	1,646	108,662	31.11%	49.10%	36.64%	44.11%	62.50%	29.42%	50.12%	67.50%	25.75%

Average Variance 38.82% Average Variance 29.51% Average Variance 26.02%

* Due to the Public Safety Realignment Act of 2011, the proper disposition of data for FY 2010-11 is not available.

CALPIA Invests in Training and Rehabilitation

FY 2013-14 Training Highlights

CALPIA invests in curriculum for offenders, including offering 108 nationally recognized accredited certifications such as dental technology, food handling, laundry, agriculture, welding, metal stamping, industrial safety and health, electrical systems, mechanical systems and maintenance. CALPIA offenders may also earn certificates of proficiency in occupational disciplines to validate skills and abilities obtained during their time employed by CALPIA (see accredited certifications, below).

In FY 2013-14, 732 CALPIA offenders received a certificate of proficiency and/or Standard Occupational Code Proficiency certification and 1,361 offenders successfully completed an accredited certification program, a 70 percent increase from FY 2012-13. The major cause of this increase was primarily due to IEP opening enrollment to all CALPIA offenders into the TPC Training Systems course, 109.1 Industrial Safety and Health.

Of those that completed an accredited certification program, 71 were graduates of CALPIA's CTE program.

Accredited Certifications

American Welding Society
Gas Metal Arc Welding 1
Gas Tungsten Arc Welding 1
Gas Tungsten Arc Welding 2
Gas Tungsten Arc Welding 3

Association for Linen Management
Certified Linen Technician
Certified Washroom Technician
Certified Laundry Linen Manager

CA Department of Food & Agriculture
Artificial Insemination License
Pasteurizer License
Sampler/Weigher License

Electronics Technicians Association
Customer Service Specialist
Certified Electronics Technician
Journeyman (Industrial)

Library of Congress – Braille
Literary Transcribing
Literary Proofreading
Mathematics Transcribing
Mathematics Proofreading
Music Transcribing

National Institute of Metalworking Skills
Machining, Level I
Metal Forming, Level I
Metal Stamping, Level II

National Restaurant Association
ServSafe Essentials
ServSafe Food Handler

North American Technician Excellence

Installation and Service for:
Air Conditioning
Air Distribution
Heat Pumps
Gas Heat
Oil Heat

Overton–Forklift Operator
Warehouse Forklift
Pallet Jack Forklift
Construction Forklift

Printing Industries of America
Sheetfed Offset Press
Web Offset Press
Bindery
Pre-Press

Productivity Training Corporation
Dental Technician

Stiles Machinery Inc.
Intermediate Weeke Machining

TCP Training Systems

Type: Fundamentals/Core Competencies

(Series 100)

101 Reading Blueprints

102 Reading Schematics and Symbols

103 Mathematics in the Plant

104 Making Measurements

105 Metals in the Plant

106 Nonmetals in the Plant

107 Hand Tools

108 Portable Power Tools

109.1 Industrial Safety and Health

110 Troubleshooting Skills

TCP Training Systems (continued)

Type: Electrical Systems

(Series 200)

201 Basic Electricity and Electronics

202 Batteries and DC Circuits

203 Transformers and AC Circuits

204.1 Electrical Measuring Instruments

205.1 Electrical Safety and Protection

206 DC Equipment and Controls

207 Single Phase Motors

208 Three Phase Systems

209 AC Control Equipment

210 Electrical Troubleshooting

211 Electrical Safety – Understanding NFPA 70E

TCP Training Systems (continued)

Type: Mechanical Systems

(Series 300)

301 Basic Mechanics

302 Lubricants and Lubrication

303.1 Power Transmission Equipment

304 Bearings

305 Pumps

306 Piping Systems

307 Basic Hydraulics

308 Hydraulic Troubleshooting

309 Basic Pneumatics

310 Pneumatic Troubleshooting

TCP Training Systems (continued)

Type: Packaging Machinery

(Series 310)

311 Introduction to Packaging

312 Packaging Machinery

313 Casing Machinery

TCP Training Systems (continued)

Type: Machine Shop Practices

(Series 320)

315 Machine Shop Practice

316 Machine Shop Turning Operations

317 Machine Shop Shaping Operations

323 Machine Shop Job Analysis

324 Lathe-Turning Work Between Centers

325 Lathe-Machining Work in a Chuck

326 Basic Milling Practices

327 Indexed Milling Procedures

328 Multiple-Machine Procedures

TCP Training Systems (continued)

Type: Mechanical Maintenance Applications

(Series 340)

341 Mechanical Drive Maintenance

342 Mechanical and Fluid Drive Systems

343 Bearing and Shaft Seal Maintenance

344 Pump Installation and Maintenance

345 Maintenance Pipefitting

346 Tubing and Hose System Maintenance

347 Valve Maintenance & Piping System Protection

TCP Training Systems (continued)

Type: Building and Grounds

(Series 360)

361 Introduction to Carpentry

362 Constructing the Building Shell

363 Finishing the Building Interior

364 Structural Painting

366 Flat Roof Maintenance

367 Plumbing Systems Maintenance

375 Landscaping Maintenance

TCP Training Systems (continued)

Type: Welding

(Series 420)

416 Blueprint Reading for Welders

417 Welding Principles

418 Oxyfuel Operations

419 Arc Welding Operations

TCP Training Systems (continued)

Type: Custodial Maintenance

(Series 450)

451 Cleaning Chemicals

452 Floors and Floor Care Equipment

453 Maintaining Floors and Other Surfaces

454 Restroom Care

455 Carpet and Upholstery Care

Financial Activity of CALPIA

Financial Overview

In Fiscal Year (FY) 2013-14, revenues increased approximately $12.4M or 6.9 percent to $192.6M from increased sales in all segments.

In FY 2014-15, CALPIA predicts revenues of $199.6M, an increase of $7M from FY 2013-14 primarily from the Healthcare Facilities Maintenance (HFM) program implementation. The anticipated year-end net position will be a $0.05M increase compared to the $8.8M decrease in FY 2013-14, resulting from the ongoing implementation of the HFM program and the transfer of the $13M from the Prison Industry Revolving Fund into the State General Fund (see Significant Impacts).

Operating Revenues

CALPIA's revenues increased approximately $20M, or 11.6 percent, between FY 2012-13 and FY 2013-14. This was primarily due to a $12M increase in manufacturing (Furniture, Metal and Chemicals) and an additional $8M increase was generated by our service enterprises (Food & Beverage Packaging, Optical, and Printing.)

The FY 2014-15 CALPIA Annual Plan (AP) anticipates revenues of $199.6M, an increase of $7M, or 3.6 percent, from FY 2013-14 revenues of $192.6M and plans utilizing approximately 6,800 offender positions. CALPIA anticipates employing 775 civil service staff in FY 2014-15 AP, a 32.9 percent increase from the previous year, due to the continued implementation of the HFM program.

CALPIA Balance Sheet

Notwithstanding the challenges of FY 2013-14, CALPIA remains financially strong. The CALPIA Statements of Net Position at June 30, 2014 reflect current assets which are almost seven times greater than current liabilities and approximately 1.5 times the amount of total liabilities, which are financial indicators that CALPIA is well positioned to meet its short term and long term obligations and equally well-positioned to expand work and training opportunities for offenders.

CALPIA remains optimistic about the future of successful business enterprises, supported by a dedicated and qualified workforce, working in partnership with satisfied customers that create the best opportunities for the rehabilitation of offender workers, resulting in a safer California.

Significant Impacts

Pro Rata Payments to the State

Despite the fact that CALPIA receives no Budget Act appropriation, CALPIA must pay the State its *Pro Rata* share of costs of State services (Legislature, Department of Finance, Controller, Treasurer, etc.) The FY 2013-14 *Pro Rata* payment was $4.3M and will be $4.1M for FY 2014-15, a decrease of $0.2M.

Postemployment Benefits Other than Pensions

Under Governmental Accounting Standards Board (GASB) Statement No. 45 (GASB 45)–Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions (OPEB), the State is required to recognize the cost of retiree health benefit programs on an accrual basis rather than on a pay as you go basis. The State Controller, who administers GASB 45 accounting requirements for the State, assessed CALPIA's share of the State's net unfunded OPEB obligation is estimated at $10.2M in FY 2014-15 AP, an increase of $2.8M from $7.4M for FY 2013-14. CALPIA records these amounts as a "selling and administrative" expense on the operating statement in addition to the actual payments made for OPEB. The State does not maintain a separate pool of assets to finance future retiree healthcare benefits. As one of the few State agencies required to fund the OPEB obligation from its own proprietary fund, CALPIA actively monitors the costs of retiree health benefits in accordance with Generally Accepted Accounting Principles (GAAP) and the funding policies of the State.

As of June 30, 2014, CALPIA's balance sheet reflects a net OPEB obligation of $46.8M. CALPIA has funded this allocation through cash reserves. CALPIA is seeking authority to reinvest these set aside funds in order to minimize the future obligation through higher interest earnings.

Transfer from Prison Industry Revolving Fund to the General Fund

Penal Code section 2806 authorizes the Secretary of CDCR and the Director of the Department of Finance to order the transfer of funds from the Prison Industry Revolving Fund to the State of California General Fund if a determination is made that the balance in the fund exceeds the amount necessary to carry out the mission of CALPIA.

Significant Impacts

On May 24, 2013, it was requested by the Department of Finance that pursuant to Penal Code 2806, the State Controller's Office (SCO) transfer $13 M from the Prison Industry Revolving Fund to the General Fund in FY 2012-13. On June 21, 2013, $13M was transferred by the State Controller from the Prison Industry Revolving Fund to the Prison Industry General Fund. The transferred funds were not appropriated for CALPIAs operational expenditures; therefore CALPIA classified the $13M as restricted cash in FY 2012-13. On July 1, 2013, the $13M was transferred from the Prison Industry General Fund, to the States General Fund.

Public Safety Realignment

In October 2011, the Governor signed Assembly Bill 109, the Public Safety Realignment Act, which has reduced the population of California prisons by over 25,000 offenders over the last two years. During FY 2012-13, CDCR's institution population declined by approximately 13,000 offenders.

It was forecasted that correctional realignment would decrease CALPIAs revenue for population driven products and services (food, clothing, and laundry) by $5.5M in FY 2012-13. However, the associated revenue decrease as a result of the reduction of the offender population was somewhat mitigated by increased revenues from new institutional food product offerings. In addition, CALPIA increased its food customer base by expanding sales at the county jail level.

Application of State Sales Tax

Per the BOE, unlike any other manufacturer, CALPIA must pay sales tax on purchases of raw materials. CALPIA paid over $4.3M in Sales and Use Tax to its vendors in FY 2012-13, which is a 2 percent increase over FY 2011-12.

Cash as Designated Liabilities

CALPIA maintains cash levels to meet liabilities such as CALPIA's OPEB obligation, accrued employee vacation, and workers compensation liabilities. CALPIA will seek authority to reinvest this cash to achieve yields that would lessen the OPEB liability. In addition, Government Code Section 16310(a) authorizes the State Treasurer to transfer idle cash from other funds (not to exceed 10 percent of the fund) to meet the cash needs of the State. CALPIA is not reimbursed for lost interest when this occurs.

Declining Offender Population

On September 12, 2013, Governor Brown signed Senate Bill 105, which facilitates the reduction of offenders in existing state facilities for transfer to either private and public correctional centers in California or private and public correctional facilities outside the state. The effects of Senate Bill 105 and Assembly Bill 109, the Public Safety Realignment Act of 2011, are reducing the number of CDCR offenders that utilize CALPIA products by over 35,000 offenders. This reduction also impacts the number of offender employees that are available for employment and training in CALPIA enterprises. CALPIA is working closely with CDCR to ensure that potential CALPIA production impacts are minimized and training and employment opportunities are maximized utilizing the remaining population of offenders.

Employee Pay Restoration and Increase

To assist in achieving budget savings in FY 2012-13, excluded, non-statutory exempt as well as State Employees International Union (SEIU), and International Union of Operating Engineers (IUOE) employees were subject to the mandatory 4.62 percent reduction in pay from July 1, 2012 through June 30, 2013.

On July 1, 2013, all employees subject to this reduction received a 4.62 percent pay restoration. The estimated financial impact to CALPIA of the pay restoration in FY 2013-14 is $1.9M. Excluded, non-statutory exempt employees and SEIU members received a three percent increase to the maximum step of the salary range in each classification on July 1, 2013. The impact to CALPIA in FY 2013-14 will be approximately $1.2M. Employee pay negotiations are conducted by the California Department of Human Resources (CalHR) and are outside the control of CALPIA.

CALPIA
Quality Products ★ Changed Lives ★ A Safer California

Enterprise Highlights

Metal Products

CALPIA continues to partner with CDCR on projects associated with prison construction legislation (AB 900, Chapter 7, 2007). CALPIA is providing metal products required for new correctional facilities, including the California Healthcare Facility in Stockton, Dewitt Nelson Correctional Annex, California City Correctional Facility and several more. These products, such as therapeutic treatment modules, beds, lockers, study carrels, and tables, have custom specifications due to their use in correctional settings. CALPIA's engineering, design and production capabilities make CALPIA uniquely qualified to meet these unique needs. Metal products continued to sell well and for the second year in a row exceeding $8M in sales. In addition to our CDCR sales, CALPIA experienced a robust level of metal products demand with Caltrans and CHP. CALPIA also experienced an increase in law enforcement vehicle outfitting for several transportation van projects with CDCR along with assorted vehicle projects with other California law enforcement agencies. There was also an increase in sales of metal products to county jails.

Food and Beverage Packaging

CALPIA's Food and Beverage Packaging Enterprise experienced a sales increase of $2.7M, primarily due to the full implementation of an individual packaged meal enterprise in FY 2013-14. In April 2012, the PIB authorized individual pre-packaged meals as a CALPIA product. This product eliminates CDCR staff time and the costs associated with individual meal assembly. CALPIA is currently providing over 500,000 individual packaged meals per month to CDCR.

Furniture Products

Furniture products experienced a $2.7M increase (+20%) over FY 12-13. Unlike FY 12-13 sales that were driven primarily by CDCR and California Veteran's Homes, the FY 13-14 volume was more diversified and largely driven by our seating volume which represented nearly 80 percent of total furniture sales.

Optical
Fiscal Year 2013-14 experienced an annual increase of approximately 110,000 new RX orders as a result of the Children of Healthy Families transitioning into Medi-Cal. This is the main reason for the increase in revenue from 10.5 million to 13 million.

Healthcare Facilities Maintenance
In FY 2013-14, in partnership with California Correctional Health Care Services (CCHCS), CALPIA established a Healthcare Facilities Maintenance (HFM) at all 34 CDCR institutions statewide. CALPIA offers a sustainable model that is well situated to meet healthcare facility maintenance needs.

HFM prepares offenders for post-incarceration employment through the accredited program, TPC Training Systems, which provides various certifications. CALPIA expects to employ over 1,000 offenders in this enterprise.

E-Waste Pilot
In July 2013, CALPIA began a vocational e-waste program to collect and facilitate recycling and refurbishment of computers and to assess the viability of establishing an e-waste recycling enterprise. The establishment of this enterprise will provide a solution for our customers and will provide valuable training to female offenders in the program. CALPIA initiated a vocational e-waste program at CALPIA's distribution warehouse facility in Sacramento. The program supports the Governor's and Legislature's goal of 75 percent recycling, composting or source reduction of solid waste by 2020. If the pilot succeeds, CALPIA will seek PIB approval to establish a statewide e-waste enterprise.

New Products

Furniture and Metal Products for Correctional Institutions and Healthcare Facilities
In support of CDCR institutions and healthcare facilities, CALPIA has continued to provide major project support and the development of numerous custom products in FY 2013-14. With the unique specifications of these facilities and the specialized manufacturing experience of CALPIA we have designed and manufactured over 30 new products for the new California Healthcare Facility, Dewitt Nelson Correctional Annex, California City Correctional Facility, and numerous large projects at other CDCR institutions throughout the fiscal year. Some of the products include stainless steel benches, treatment modules and mess tables.

Bindery Products
In partnership with Caltrans, CALPIA developed new Retro-reflective roadwork signs. Retro-reflective signs improve highway safety and night-time visibility for drivers. CALPIA received initial orders at the end of FY 13-14 totaling $900,000 with annual orders to follow.

New Custom Furniture for the Department of Military
In FY 13-14, CALPIA contracted with the Department of the Military to build and install custom metal dorm products in 25 barracks at Camp Roberts in San Luis Obispo County. This CALPIA major project ($1.5M) is a key part of the major Camp Roberts renovation project slated to be completed in 2016.

Improved Processes

Improved Customer Service

The CALPIA customer feedback portal has allowed CALPIA to improve the customer experience by monitoring the feedback portal on a daily basis. CALPIA has been able to improve response times with timely solutions and ultimately making our customer service department more efficient. We continue to provide training to all sales and customer service staff to assist in managing customer relationships and projects to ensure the ultimate customer experience.

Quality Control and International Organization for Standards (ISO)

In FY 2013-14, CALPIA reviewed and updated International Organization for Standards (ISO) policy and procedure documentation. ISO is the world's largest developer and publisher of international standards. A surveillance audit was conducted in December 2013 by an external ISO auditor and it verified that CALPIA maintained an effective quality system. Also, in FY 2013-14, CALPIA initiated and resolved 45 corrective action plans that further confirmed the commitment to customer focus and continuous improvement. Additionally, the cleaning products enterprise became ISO certified in December 2013.

CALPIA is one of two state correctional industries in the nation that is ISO certified. Implementing and maintaining quality standards affirms CALPIA's commitment to producing superior products while maintaining effective customer service. In FY 2014-15, CALPIA will be seeking ISO certification for laundry services, dairy and food and beverage packaging enterprises.

Lean Manufacturing and Kaizen

CALPIA continues training and implementation of Lean Manufacturing and Kaizen in various enterprises. Lean Manufacturing is a process improvement system that identifies and eliminates waste, understands customer needs, analyzes business processes and institutes proper measurement methods. Kaizen is a Japanese word, meaning, "many small improvements" and was developed by Japan's Kaizen Institute.

As of June 30, 2014, six enterprises (three furniture locations, two metal locations and general fabrication) have received Lean Practitioner Training and began Lean Phase 1. Eight fabric locations enrolled in the Lean Practitioner Training.

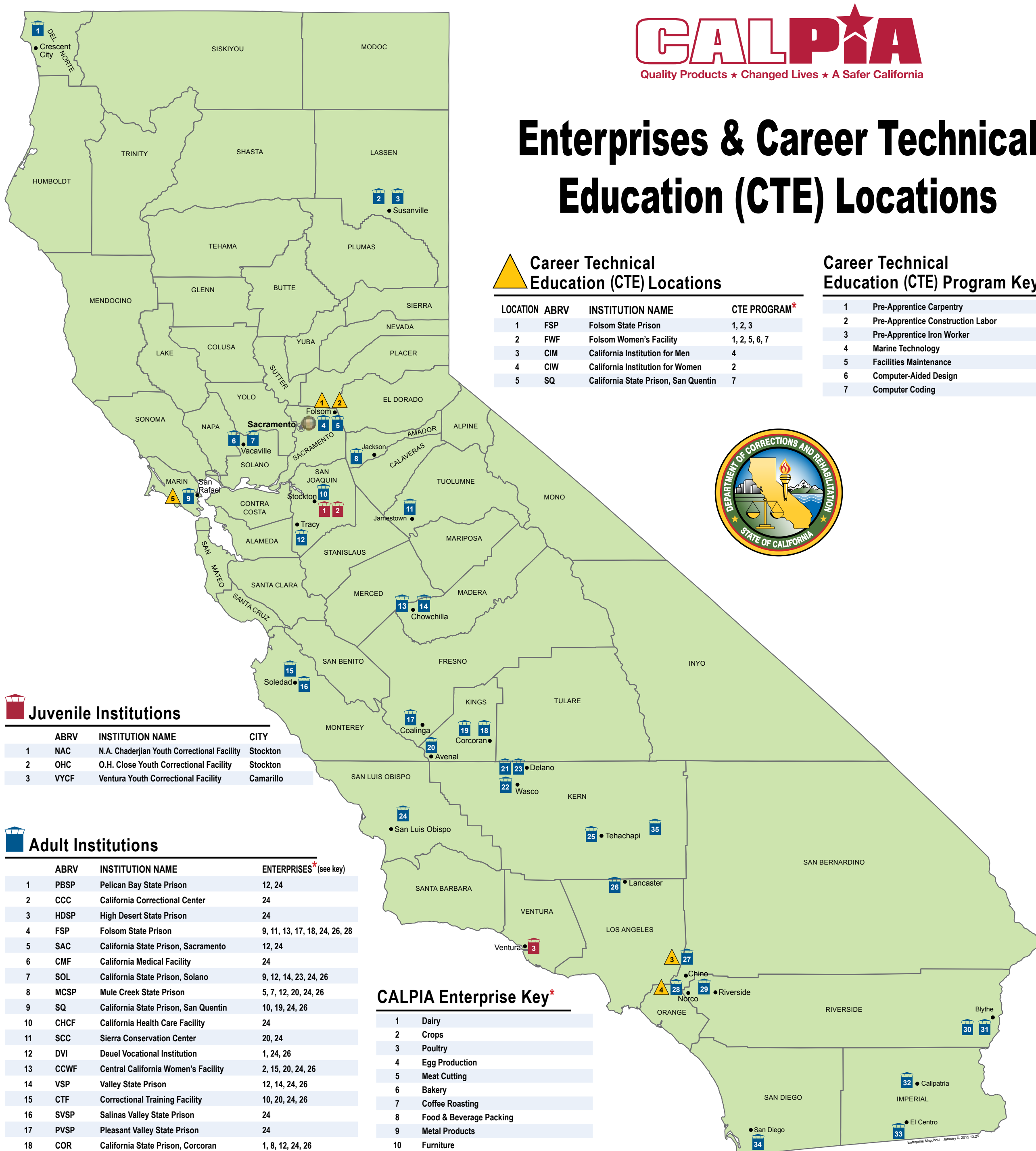
PIB Meetings - Summary of Action Items Calendar Year 2014

Meeting	Item	2014
1/29/14	[14-0129-351-AI]	A. Approval of the California Prison Industry Authority's Report to the Legislature Fiscal Year 2012-2013
	[14-0129-352-AI]	B. Approval of Prison Industry Board Procedural Rules
	[14-0129-353-AI]	C. Approval of Establishment of a Vice Chair Position
6/25/14	[14-0625-306-AP]	A. Adoption of the Annual Plan for the Fiscal Year 2014/2015
	[14-0625-307-AP]	B. Designation of Cash for the Fiscal Year 2014/2015
	[14-0625-354-AI]	C. Amend Regulations of Title 15, Division 8, Article 1 & Adoption of Regulations Title 15, Division 8, New Article 6 Concerning CALPIA Personnel Sections 8000, 8100, 8101, 8102, 8103, 8104, 8105, 8106, 8107, 8108, 8109, 8110, 8111, 8112, 8113, 8114, 8115, 8116, 8117, 8118, 8119, 8119.1, and 8120
12/18/14	[14-1218-355-AI]	A. Addition of Food & Beverage Packaging Enterprise at Mule Creek State Prison
	[14-1218-356-AI]	B. Increase Revenue Limit of Construction Services and Facilities Maintenance Statewide
	[14-1218-308-AP]	C. Adoption of Fiscal Year 2014-15 Proposed Mid-Year Revise
	[14-1218-357-AI]	D. Adoption of Regulations Title 15, Division 8, Article 6 CALPIA Personnel Section 8121
	[14-1218-358-AI]	E. Adoption of Regulations Title 15, Division 8, Article 3 CALPIA Inmate Recruitment and Hiring Processes Sections 8004, 8004.2, 8004.3, 8004.4, and 8005

CALPIA Enterprises by Location

CALPIA
Quality Products ★ Changed Lives ★ A Safer California

Enterprises & Career Technical Education (CTE) Locations



Career Technical Education (CTE) Locations

LOCATION	ABRV	INSTITUTION NAME	CTE PROGRAM*
1	FSP	Folsom State Prison	1, 2, 3
2	FWF	Folsom Women's Facility	1, 2, 5, 6, 7
3	CIM	California Institution for Men	4
4	CIW	California Institution for Women	2
5	SQ	California State Prison, San Quentin	7

Career Technical Education (CTE) Program Key*

1	Pre-Apprentice Carpentry
2	Pre-Apprentice Construction Labor
3	Pre-Apprentice Iron Worker
4	Marine Technology
5	Facilities Maintenance
6	Computer-Aided Design
7	Computer Coding

Juvenile Institutions

	ABRV	INSTITUTION NAME	CITY
1	NAC	N.A. Chaderjian Youth Correctional Facility	Stockton
2	OHC	O.H. Close Youth Correctional Facility	Stockton
3	VYCF	Ventura Youth Correctional Facility	Camarillo

Adult Institutions

	ABRV	INSTITUTION NAME	ENTERPRISES* (see key)
1	PBSP	Pelican Bay State Prison	12, 24
2	CCC	California Correctional Center	24
3	HDSP	High Desert State Prison	24
4	FSP	Folsom State Prison	9, 11, 13, 17, 18, 24, 26, 28
5	SAC	California State Prison, Sacramento	12, 24
6	CMF	California Medical Facility	24
7	SOL	California State Prison, Solano	9, 12, 14, 23, 24, 26
8	MCSP	Mule Creek State Prison	5, 7, 12, 20, 24, 26
9	SQ	California State Prison, San Quentin	10, 19, 24, 26
10	CHCF	California Health Care Facility	24
11	SCC	Sierra Conservation Center	20, 24
12	DVI	Deuel Vocational Institution	1, 24, 26
13	CCWF	Central California Women's Facility	2, 15, 20, 24, 26
14	VSP	Valley State Prison	12, 14, 24, 26
15	CTF	Correctional Training Facility	10, 20, 24, 26
16	SVSP	Salinas Valley State Prison	24
17	PVSP	Pleasant Valley State Prison	24
18	COR	California State Prison, Corcoran	1, 8, 12, 24, 26
19	SATF	Substance Abuse Treatment Facility	8, 24
20	ASP	Avenal State Prison	3, 4, 10, 12, 24, 25, 26
21	NKSP	North Kern State Prison	24
22	WSP	Wasco State Prison	12, 24
23	KVSP	Kern Valley State Prison	24
24	CMC	California Men's Colony	12,17, 20, 21, 22, 24, 26
25	CCI	California Correctional Institution	20, 24, 26
26	LAC	California State Prison, Los Angeles County	12, 16, 24, 26
27	CIM	California Institution for Men	8, 12, 24, 26
28	CIW	California Institution for Women	20, 24
29	CRC	California Rehabilitation Center	24
30	CVSP	Chuckawalla Valley State Prison	12, 24
31	ISP	Ironwood State Prison	24
32	CAL	Calipatria State Prison	24
33	CEN	Centinela State Prison	20, 24
34	RJD	RJ Donovan Correctional Facility	6, 12, 22, 24, 26
35	CAC	California City Correctional Facility	24

CALPIA Enterprise Key*

1	Dairy
2	Crops
3	Poultry
4	Egg Production
5	Meat Cutting
6	Bakery
7	Coffee Roasting
8	Food & Beverage Packing
9	Metal Products
10	Furniture
11	License Plates
12	Laundry
13	Digital Services
14	Optical
15	Dental lab
16	Cleaning Products
17	Printing
18	Metal Signs
19	Mattress
20	Fabric Products
21	Knitting Mill
22	Shoes
23	Bindery
24	Construction Services Facilities Maintenance
25	General Fabrication/Century
26	Support Services
27	On Time Delivery Center
28	Modular Building

CDCR Headquarters

Department of Corrections and Rehabilitation
1515 "S" Street
Sacramento, CA 95814

CALPIA Central Office

560 East Natoma Street
Folsom, CA 95630-2200

Financial Overview

Financial Plan (In Thousands)	FY 2012-13 Actuals*	FY 2013-14 Actuals*	FY 2014-15 Approved Annual Plan	FY 2014-15 Approved Mid-Year Revise
Revenues				
Manufacturing	$85,712	$86,222	$76,745	$80,745
Services	66,987	77,855	93,649	92,995
Agricultural	27,547	28,566	25,871	25,871
Total Revenue	**$180,246**	**$192,643**	**$196,265**	**$199,611**
Expenses				
Cost of Goods Sold				
Manufacturing	$64,157	$63,814	$55,561	$57,250
Services	48,932	53,610	68,103	70,473
Agricultural	25,428	26,643	22,979	22,960
Total Cost of Goods Sold	$138,517	$144,067	$146,643	$150,683
Gross Profit	**$41,729**	**$48,576**	**$49,622**	**$48,928**
Selling and Administration				
Central Office				
Prison Industry Board	$128	$82	$188	$191
Executive Management	287	309	390	374
Legal	607	603	638	633
External Affairs	141	125	144	159
Operations Division	3,029	4,524	3,472	3,420
Marketing Division	3,480	3,525	3,922	3,841
Administration Division				
Administration Mgmt	109	373	235	195
Business Services	820	807	1,254	1,231
Management Information Systems	2,858	3,865	3,741	3,782
Human Resources	1,005	1,229	1,289	1,429
Staff Development	427	586	1,007	927
Health & Safety	294	535	480	507
Finance Division	2,604	2,556	3,222	3,408
Sub-total Central Office	$15,789	$19,119	$19,982	$20,097
Offender Development Programs				
Industry Employment Program	$536	$720	$1,343	$1,344
Reimbursement	0	0	0	0
Joint Venture/Free Venture	383	648	668	668
Reimbursement	(651)	(656)	(668)	(668)
Career Technical Education	1,070	1,714	2,644	2,941
Reimbursement	0	(1,989)	(2,211)	(2,211)
Total Offender Development Programs	$1,338	$437	$1,776	$2,074
Distribution/Transportation	$12,119	$12,873	$12,018	$12,203
State Pro Rata	4,789	4,269	4,958	4,068
Other Post Employment Benefits	7,191	7,359	10,240	10,240
Total Selling and Administration	**$41,226**	**$44,057**	**$48,974**	**$48,682**
Operating Income/(Loss)	**$503**	**$4,519**	**$648**	**$246**
Non-Operating Revenues/Expenses	($586)	($319)	($200)	($200)
Penal Code 2806 Transfer	$0	($13,000)	$0	$0
Net Gain/(Loss)	**($83)**	**($8,800)**	**$448**	**$46**

* For the purpose of this section, the display of audited financial information was reconfigured to remove Pro Rata Costs for each category. A State Pro Rata category was added to display associated costs. The Net Gain (Loss) of the fiscal year equals the audited financial statement.

Enterprise Overview (In Thousands)	Revenue	Cost of Goods Sold	Gross Profit (Loss)
Manufacturing			
Furniture	$16,500	$11,666	$4,834
Metal Products	6,000	5,025	975
License Plates	15,500	7,219	8,281
General Fabrication	6,600	5,859	741
Bindery	2,600	1,645	955
Knitting Mill	1,384	957	427
Fabric Products	18,902	14,979	3,923
Shoes	4,009	3,219	790
Mattresses	2,450	1,967	483
Cleaning Products	6,800	4,431	2,369
Modular Construction	0	283	(283)
Sub-total Manufacturing	**$80,745**	**$57,250**	**$23,495**
Services			
Meat Cutting	$11,435	$9,409	$2,026
Bakery	3,297	2,113	1,184
Coffee Roasting	1,668	1,429	239
Food & Beverage Packaging	21,660	18,166	3,494
Metal Signs	1,350	912	438
Printing	5,100	2,865	2,235
Dental Lab	700	442	258
Digital Services	500	349	151
Laundry	13,348	10,200	3,148
Optical	12,000	6,210	5,790
Construction Services & Facilities Maintenance	21,937	18,378	3,559
Sub-total Services	**$92,995**	**$70,473**	**$22,522**
Agricultural			
Dairy / Farm	$12,835	$11,312	$1,523
Crops	532	847	(315)
Poultry	5,910	5,437	473
Egg Production	6,594	5,364	1,230
Sub-total Agricultural	**$25,871**	**$22,960**	**$2,911**
Total	**$199,611**	**$150,683**	**$48,928**

Offender Assignments by Enterprise

Offender Assignments	FY 2012-13 Actuals	FY 2013-14 Actuals	FY 2014-15 Approved Annual Plan	FY 2014-15 Approved Mid-Year Revise
Manufacturing				
Furniture	410	465	508	508
Metal Products	216	221	240	240
License Plates	104	105	116	116
General Fabrication	138	110	138	138
Bindery	69	51	105	105
Knitting Mill	63	60	120	120
Fabric Products	1,224	1,124	1,461	1,461
Shoes	130	121	170	170
Mattresses	39	35	111	111
Cleaning Products	50	44	54	54
Modular Construction	50	32	66	66
Sub-total Manufacturing	**2,493**	**2,368**	**3,089**	**3,089**
Services				
Meat Cutting	63	60	75	75
Bakery	59	46	52	52
Coffee Roasting	23	22	25	25
Food & Beverage Packaging	169	174	147	206
Metal Signs	36	38	33	33
Printing	124	111	131	131
Dental Lab	56	56	56	56
Digital Services	16	17	18	18
Laundry	662	633	787	787
Optical	190	188	190	190
Construction Services & Facilities Maintenance	97	220	941	987
Sub-total Services	**1,495**	**1,565**	**2,455**	**2,560**
Agricultural				
Dairy / Farm	185	157	236	236
Crops	14	13	48	48
Poultry	25	31	31	31
Egg Production	28	23	48	48
Sub-total Agricultural	**252**	**224**	**363**	**363**
Selling and Administration				
Statewide Administrative Support	261	222	369	366
On-Time Delivery	26	24	28	31
Central Office	10	31	44	44
Career Technical Education Programs	43	96	348	348
Sub-total Selling and Administration	**340**	**373**	**789**	**789**
Total	**4,580**	**4,530**	**6,696**	**6,801**

Inmate Positions by Location

Location	Average Monthly Filled Inmate Assignments		
	FY 2011-12	FY 2012-13	FY 2013-14
California Institution for Men	210	207	190
California Men's Colony	593	557	538
R. J. Donovan Correctional Facility	206	167	184
Correctional Training Facility	360	363	381
Avenal State Prison	423	390	420
Deuel Vocational Institution	106	69	65
Folsom State Prison	449	392	397
CSP Sacramento	33	34	26
FWF/OTD North	9	9	71
San Quentin State Prison	172	130	149
California Institution for Women	102	112	108
California Correctional Institution	255	247	220
California State Prison, Solano - includes CMF	393	385	380
Mule Creek State Prison	348	343	334
Corcoran State Prison/Substance Abuse Treatment Facility	338	348	347
Chuckawalla Valley State Prison	37	32	44
Pelican Bay State Prison	18	17	16
Sierra Conservation Center	125	131	141
Central California Women's Facility/Valley State Prison	397	339	290
California State Prison, Lancaster	97	91	76
Wasco State Prison	76	67	55
Centinela State Prison	70	70	73
Central Office	23	17	22
Total	**4,870**	**4,517**	**4,527**

CALIFORNIA PRISON INDUSTRY AUTHORITY

(A Component Unit of the

State of California)

ANNUAL FINANCIAL REPORT

For the Fiscal Years Ended June 30, 2014 and 2013

CALIFORNIA PRISON INDUSTRY AUTHORITY
(A Component Unit of the State of California)

Table of Contents

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3000 S Street, Suite 300
Sacramento, CA 95816
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Walnut Creek

Oakland

LA/Century City

Newport Beach

San Diego

Seattle

INDEPENDENT AUDITOR'S REPORT

To the California Prison Industry Authority Board
Folsom, California

Report on the Financial Statements

We have audited the accompanying financial statements of California Prison Industry Authority ("CALPIA"), a component unit of the State of California, as of June 30, 2014 and 2013, and the related statements of revenues, expenses, and changes in net position and cash flows for the fiscal years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether by fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of CALPIA as of June 30, 2014 and 2013, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 15 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers 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.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 5, 2014 on our consideration of CALPIA's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants agreements and other matters The purpose of that report 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. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering CALPIA's internal control over financial reporting and compliance.

Macias Gini & O'Connell LLP

Sacramento, California
November 5, 2014

CALIFORNIA PRISON INDUSTRY AUTHORITY

The following Management Discussion and Analysis (MD&A) applies only to the activities of the California Prison Industry Authority (CALPIA) and should be read in conjunction with its financial statements and related footnotes.

CALPIA is a proprietary component unit of the State of California (State) and is accounted for in the Prison Industries Revolving Fund, which is an internal service fund in the State's basic financial statements. CALPIA does not receive a General Fund appropriation.

Chapter 1549, Statutes of 1982, created CALPIA as a self-supporting state agency. The statutory purposes of the CALPIA are to:

- Develop and operate manufacturing, service, and agricultural enterprises that provide work opportunities for offenders under the jurisdiction of the California Department of Corrections and Rehabilitation ("CDCR");

- Create and maintain working conditions within enterprises, as much like those which prevail in private industry as possible, to assure offenders the opportunity to work productively to earn wages, and to acquire or improve effective work habits or occupational skills;

- Operate a work program for offenders that is self-supporting through the sale of products and services, and reduces the cost of operations of the CDCR.

CALPIA is under the policy direction of an eleven-member board of directors, which reviews and approves the annual budget for the CALPIA. CALPIA manages 27 manufacturing, service, and agricultural business lines which includes 73 enterprises/factories. Administrative offices are located in Folsom, California. The goods and services produced by CALPIA's operations are sold principally to departments of the State of California, and other governmental entities. CDCR is CALPIA's largest customer, and accounted for 57.1% and 57.4% of all sales in the fiscal years ended June30, 2014 and 2013, respectively.

Overview of the Financial Statements

The financial statements presented herein include all of the activities of CALPIA as prescribed by statements of the Governmental Accounting Standards Board (GASB).

The Statements of Net Position include all assets and liabilities of CALPIA. They are prepared under the accrual basis of accounting, whereby revenues and receivables are recognized when the service is provided and expenses and liabilities are recognized when incurred, regardless of when cash is exchanged.

The Statements of Revenues, Expenses and Changes in Net Position, present information reflecting how net position changed during the most recent two fiscal years. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in the statement for some items that will result in cash flows in future fiscal periods (e.g., uncollected service charges and earned but unused vacation leave).

The Statements of Cash Flows present information about the cash receipts and cash payments of CALPIA during the two most recent fiscal years. When used with related disclosures and information in the other financial statements, the information provided in these statements should help financial report users assess CALPIA's ability to generate future net cash flows, its ability to meet its obligations as they come due, and its need for external financing. It also provides insight into the reasons for differences between operating income and associated cash receipts and payments, and the effects on CALPIA's financial position of its cash and its noncash investing, capital, and related financing transactions during the year.

Notes to the Basic Financial Statements provide additional information that is essential to a full understanding of the data provided in CALPIA's basic financial statements. The notes are included immediately following the basic financial statements within this report.

Financial Overview

CALPIA has consistently ensured self-sufficiency through the implementation of strategic planning processes and cost containment measures to fulfill its statutory requirement of self-sufficiency.

CALPIA experienced a $12.4 million increase in operating revenues in fiscal 2014 due, in part, to increased revenues in its services enterprises from optical billing for services provided to Medi-Cal for the Healthy Families optical beneficiaries, as well as from meat cutting, coffee roasting, food and beverage packaging, and the Health Care Facilities Maintenance program that was activated in fiscal 2014. In manufacturing enterprises, sales in furniture, mattress, and cleaning products increased, while demand for metal, bindery, and fabric products declined.

Gross profits have increased for several CALPIA business lines due to an increase in business for major projects as well as new centralized procurement processes for various food related raw materials which has optimized CALPIA's ability to purchase and achieve volume quantity discounts at best value. Gross profits have been impacted for other CALPIA business lines, in part due to the declining CDCR offender population.

CALPIA recorded a loss (decrease) in net position of $8.8 million and $0.1 million during fiscal years 2014 and 2013 respectively. The primary factor related to the decrease in net position for fiscal 2014 is due to the increase in Non-Operating Expenses of $12.9 million. This was attributable to the transfer of $13.0 million from the Prison Industry Revolving Fund to the Prison Industry General Fund at the request of the California Department of Finance in accordance with California's Penal Code Section 2806. The $13.0 million was classified as restricted cash at June 30, 2013. The transfer also reduced restricted cash, thereby reducing its net position. In addition, net position was impacted by a $1.8 million increase in worker's compensation reserve and an increase of $7.4 million for Other Post-Employment Benefits (OPEB). Notwithstanding the transfer of funds from CALPIA which affected our net position, CALPIA remains financially strong. The CALPIA Statements of Net Position at June 30, 2014 reflects current assets are almost seven times greater than current liabilities and approximately 1.5 times the amount of total liabilities, which are financial indicators that CALPIA is well positioned to meet its short term and long term obligations. If not for the Department of Finance transfer of $13.0 million, CALPIA would have been profitable in fiscal 2014.

Transfer from Prison Industry Revolving Fund to the General Fund

Penal Code section 2806 authorizes the Secretary of CDCR and the Director of the Department of Finance to request the transfer of funds from the Prison Industry Revolving Fund to the General Fund if a determination is made that the balance in the fund exceeds the amount necessary to carry out the statutory purpose of CALPIA. In fiscal 2013, in conjunction with such determination, $13.0 million was transferred from the Prison Industry Revolving Fund to the CALPIA General Fund and was classified as restricted cash. In fiscal 2014, the funds were transferred to the State of California General Fund and CALPIA recognized the $13.0 million reduction in restricted cash, thereby reducing assets.

Public Safety Realignment

In October of 2011, the Governor signed AB 109, the Public Safety Realignment Act, mandating the transfer of low risk offenders to county and local jails. The reduction in the number of offenders did not initially decrease revenue as originally anticipated due to extensions granted by the United States federal court at the request of the State of California as well as an increase in products sold to CDCR for consumption. However, during fiscal year 2014, there was a decrease in revenue of approximately $0.8 million related to AB 109 It is anticipated that AB 109 will continue to have a negative impact on CALPIA's revenues in fiscal 2015 as CDCR's prison population continues to decrease. In order to maintain financial sustainability, CALPIA will continue to research and develop new products and services for its customers.

Pro Rata Payments to State

By law, CALPIA must pay the State its pro rata share of costs of State services including the Legislature, Department of Finance, State Controller Office, State Treasurer's Office, etc. Pro rata expenses are based on the allocation the Department of Finance sets for CALPIA each fiscal year. CALPIA's pro rata payment of $4.3 million in fiscal 2014, is down from $4.8 million in fiscal 2013.

Postemployment Benefits Other than Pensions

Under Governmental Accounting Standards Board (GASB) Statement No. 45 (GASB 45)—Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions (OPEB), the State is required to recognize the cost of retiree health benefit programs on an accrual basis rather than on a pay as you go basis. The State Controller, who administers GASB 45 accounting requirements for the State, assessed that CALPIA's share of the State's OPEB cost is $7.4 and $7.2 million for the fiscal years 2014 and 2013, respectively. CALPIA recorded these amounts as selling and administrative expense on the operating statement in addition to the actual payments made for OPEB. The State does not maintain a separate pool of assets to finance future retiree healthcare benefits. As one of the few State agencies required to fund the OPEB obligation from its own proprietary fund, CALPIA actively monitors the costs of retiree health benefits in accordance with Generally Accepted Accounting Principles and the funding policies of the State. As of June 30, 2014, CALPIA's balance sheet reflects a net OPEB obligation of $46.8 million. CALPIA is seeking authority to restrict an equivalent amount of cash in order to meet future obligations.

Employee Pay Restoration and Pay Increase

Effective July 1, 2014, California Department of Human Resources approved a 2.0% general salary increase for excluded, non-statutory exempt employees and State Employees International Union (SEIU) members and a one-time bonus of $1,200 for International Union of Operating Engineers (IUOE) members. The estimated impact to CALPIA salary expenses in fiscal 2015 is $1.9 million. Effective July 1, 2015 SEIU and IUOE members will receive a 2.5% and 3.0% salary increase respectively, with an estimated impact of $1.0 million.

To assist in achieving budget savings in fiscal 2013, excluded, non-statutory exempt, as well as SEIU, and International Union of Operating Engineers employees were subject to the mandatory 4.6% reduction in pay from July 1, 2012 through June 30, 2013. On July 1, 2013, all employees subject to this reduction received a 4.6% pay restoration. The estimated financial impact to CALPIA of the pay restoration in fiscal 2014 was approximately $2.0 million. Employee pay negotiations are conducted by the California Department of Human Resources and are outside the control of CALPIA. Excluded, non-statutory exempt employees and SEIU members received a 3.0% increase to the maximum step of the salary range in each classification on July 1, 2013, resulting in an increase of approximately $1.3 million in fiscal 2014.

Factory Closures

In fiscal 2014 and 2013, CALPIA had no factory closures.

CALPIA Overview

CALPIA is financially resilient because management adjusts to the ever-changing business and governmental environment in which it operates in conjunction with the CALPIA Strategic Business Plan. The emphasis of this Plan is the dual priority of providing inmate rehabilitation and operating a self-sufficient business. The Plan enumerates strategic goals, objectives, and initiatives to accomplish CALPIA's mission.

CALPIA continues to partner with CDCR on projects associated with prison construction. CALPIA provided numerous metal and furniture products required for new correctional healthcare facilities. These products such as beds, lockers, and tables have custom specifications designed for use in correctional settings. CALPIA's production experience and capabilities make CALPIA uniquely qualified to meet CDCR's needs.

CALPIA has continued to work with the California Department of Forestry and Fire Protection (CAL FIRE), to improve the line of wild land fire protection clothing designed to the unique specifications of CAL FIRE. Additionally, as a result of the ongoing partnership with the California Department of Transportation (Caltrans), CALPIA continues to improve and design clothing that meets the American National Standards Institute (ANSI) requirements for Caltrans employees.

CALPIA introduced pre-packaged lunches in fiscal 2013 and sales increased $2.7 million (13.5%) in fiscal 2014. The pre-packaged lunch consisting of sliced bread, peanut butter, jelly, cookies, almonds and drink mixes provide an effective way for CDCR institutions to feed their offenders. These lunches are also a key resource for handling emergency situations such as lockdowns.

In fiscal 2014, CALPIA endeavored to enhance the application of International Organization for Standardization (ISO) principles through a systematic internal auditing of all ISO-certified departmental units and factories. Audit results indicate that the ISO quality management system is well-implemented. Other auditing activities included the ABS Quality Evaluations, Inc., surveillance audit of existing ISO-certified units and factories, and an expansion audit of CALPIA's Cleaning Products factory, bringing our count of ISO-certified enterprises to sixteen. Fiscal 2013 was characterized by CALPIA's on-going efforts to adapt to market conditions and improve the overall quality of its products and services. These efforts included expanding the application of International Standards Organization (ISO) principles throughout the organization. In fiscal 2013, CALPIA placed emphasis on existing ISO certifications, by reviewing and updating policy and procedure documentation.

In fiscal 2015, CALPIA will continue its commitment to quality by enhancing quality management training, which focuses on ISO procedural documentation and to obtain certification of additional enterprises.

In order to improve customer service, CALPIA remains focused on improving quality and customer satisfaction through the implementation of a web-based customer feedback process originally introduced in March 2012. In fiscal 2014, customer feedback continued to be logged and routed through helpdesk software so that it could be tracked and analyzed to determine the root cause of failures, resolve customer complaints and potentially initiate ISO preventative and corrective actions. The process has benefitted CALPIA in numerous ways including improving processes, product and service quality, customer satisfaction and transparency within the organization as well as reducing costs due to quality issues.

As previously noted above, CALPIA was created to be a business enterprise to offer work employment opportunities to offenders incarcerated in state institutions. CALPIA distinguishes itself as a state program by providing offenders work opportunities and skills they will require to re-enter society as productive citizens. In fiscal 2014, CALPIA employed approximately 8,000 offenders assigned to 6,700 positions in manufacturing, service, and agricultural enterprises. CALPIA continues to provide curricula for offenders, including 13 programs that offer nationally recognized accredited certifications such as, dental technology, food handling, laundry, agriculture, welding, and metal stamping. In fiscal 2013, CALPIA employed approximately 7,000 offenders assigned to 5,560 positions. For fiscal 2015, the Prison Industry Board approved the Annual Plan which anticipates an increase of 611 offender assignments due to the implementation of the Health Care Facilities Maintenance program.

Through fiscal 2014, CALPIA offered Career Technical Education (CTE) programs in commercial diving, carpentry, construction labor, AutoCAD, and ironworking in partnership with trade unions who offer employment possibilities when offenders are released on parole. CALPIA offenders also earn certificates of proficiency in occupational disciplines which may be utilized upon parole to validate skills and abilities acquired during employment with CALPIA. In fiscal 2014, 732 CALPIA offenders received a certificate of proficiency, and another 1,361 successfully completed an accredited certification program. In fiscal 2013, 662 CALPIA offenders received a certificate of proficiency, and another 800 successfully completed an accredited certification program.

In times of economic uncertainty, it is incumbent upon CALPIA to be as responsive as possible to customer demands. In that regard, CALPIA is proud of its contributions to the State. Research indicates that CALPIA saves the State money, both by enhancing the safety of prisons, which helps to reduce staffing costs and by demonstrating lower recidivism rates among those offenders who work in its programs. The recidivism rate of CALPIA offenders is 26% to 38% lower than general population offenders and even less for CALPIA offenders participating in CTE programs. Although other factors may contribute to lower recidivism, incarceration cost avoidance from CALPIA industries saves the California State General Fund approximately $8.5 million per year (Bureau of State Audits, May, 2011).

CALPIA must focus on issues which directly affect its ability to operate a business in a correctional environment. Governor Brown signed Senate Bill 105 (Chapter 310/2013), which facilitates the reduction of offenders in existing state facilities for transfer to either private facilities in California or correctional facilities outside the state. The effects of this and AB 109, the Public Safety Realignment Act of 2011, will reduce the number of CDCR offenders that CALPIA produces products for by over 35,000 offenders, thus impacting the number of offender employees that are available to service CALPIA enterprises.

As our customers benefit from quality goods and services, so do our offender workers and, ultimately communities throughout California. CALPIA remains optimistic about a future of successful business enterprises, supported by a dedicated and qualified workforce, working in partnership with satisfied customers that create the best opportunities for the rehabilitation of offender workers.

Condensed Statements of Net Position

The following table presents the condensed statements of net position for CALPIA as of June 30, 2014, 2013 and 2012:

	2014	2013	2012
ASSETS			
Cash and cash equivalents	$ 83,634,684	$ 66,718,853	$ 70,838,529
Restricted cash	-	13,000,000	-
Accounts receivable	10,159,363	11,515,315	8,735,239
Due from State General Fund	-	-	-
Inventories	37,804,684	40,808,675	41,693,682
Capital assets, net	45,137,731	42,983,821	44,565,093
other	281,671	180,628	260,103
Total Assets	$ 177,018,133	$ 175,207,292	$ 166,092,646
LIABILITIES AND NET POSITION			
Accounts payable and accrued Liabilities	$ 25,187,483	$ 22,687,293	$ 21,278,485
Unearned revenues	895,972	1,984,609	1,686,676
Workers' compensation liability	17,682,000	15,841,448	15,541,448
Net OPEB obligation	46,808,000	39,449,000	32,258,000
Total Liabilities	90,573,455	79,962,350	70,764,609
Net Position			
Net investment in capital assets	45,137,731	42,983,821	44,565,093
Restricted	-	13,000,000	-
Unrestricted	41,306,947	39,261,121	50,762,944
Total Net Position	86,444,678	95,244,942	95,328,037
TOTAL LIABILITIES AND NET POSITION	$ 177,018,133	$ 175,207,292	$ 166,092,646

Assets

Total assets increased by $1.8 million at June 30, 2014 when compared to June 30, 2013. This results from a $3.9 million increase in cash and cash equivalents and a $2.2 million increase in capital assets, offset by $1.3 million decrease in accounts receivable, and $3.0 million decrease in inventories. In fiscal 2013, the $2.8 million increase in accounts receivable at June 30, 2013 resulted primarily from a $2.6 million increase in receivables related to the sale of capital goods.

In fiscal 2014, the $3.9 million increase in cash and cash equivalents, including designated cash is explained by an increase of $3.3 million from capital and related financing activities and $12.4 million cash provided by operating activities less $8.6 million for net capital asset acquisitions. In fiscal 2014, CALPIA recognized the transfer of $13.0 million from the Prison Industry General Fund to State of California General Fund.

In fiscal 2013, the $8.9 million increase in cash and cash equivalents, including designated and restricted cash, was explained by $0.2 million investing activities and $14.0 million cash provided by operating activities less $5.3 million for net capital asset acquisitions. In accordance with the California Penal Code Section 2806, at the request of the Department of Finance, the California State Treasurer's Office directed a transfer of $13.0 million from CALPIA's Prison Industry Revolving Fund to the State of California's General Fund. As the transfer was not effected as of June 30, 2013, these funds were classified as restricted cash by CALPIA.

In fiscal 2014, the $3.0 million decrease in inventories resulted from implementing lean manufacturing in several of CALPIA's manufacturing enterprises. The increase in capital assets is mainly attributable to the acquisition of equipment and the construction of the new Business Services building at CALPIA headquarters.

In fiscal 2013, the $0.9 million decrease in inventories was primarily attributable to inventory expense adjustments relating to obsolete inventory and lower of cost or market valuation. The decrease in capital assets of $1.6 million is mainly attributable to the depreciation of fixed assets and the disposal of obsolete equipment.

Liabilities

Total liabilities increased by $10.6 million at June 30, 2014 when compared to June 30, 2013. This is explained primarily by a $7.4 million increase in the net liability for OPEB, $2.5 million increase in accounts payable and accrued liabilities, $1.8 million increase in Worker's Compensation liability, and $1.1 million decrease in deferred revenues.

The State annually allocates a portion of retiree health benefit costs to the Prison Industries Revolving Fund. The State recognizes the annual contribution to the plan based on an actuarial valuation that estimates the present value of future retiree healthcare benefits earned during the employee's working lifetime, including an amortization of the value of unfunded retiree healthcare benefits attributable to employee service earned in prior fiscal years. The State Controller's Office has determined that CALPIA's annual required OPEB contribution is $11.2 million for fiscal 2014. Of this amount, CALPIA contributed $4.0 million; the balance of $7.4 million increased the net OPEB long term liability. CALPIA's annual required OPEB contribution for fiscal 2013 was $11.1 million. Of this amount, CALPIA contributed $ 3.9 million; the balance of $ 7.2 million increased the net OPEB long term liability.

Under current accounting rules, CALPIA is obligated to record as a liability any difference between its annual pension cost and its annual contribution amount. Historically, CALPIA has covered the fully funded annual pension cost.
In accordance with GASB No. 68, CALPIA anticipates that effective June 30, 2015, it will have to accrue its actuarially determined unfunded pension obligation. As CALPIA participates in the State of California's multi-employee pension system, it is unable to determine the specific impact on its net position at this time. However, it believes that the effect is potentially material to its net position.

In fiscal 2014, the $2.5 million increase in accounts payable and accrued liabilities is primarily attributable to a delay in the State Controller's Office (SCO) processing CALPIA claim schedules which increased the liability by $1.0 million, $0.9 million increase in accounts payable accruals, and $0.5 million increase in accrued personal services leave.

The fiscal 2014, the $1.8 million increase for Worker's Compensation liability is attributable to the payroll increase due to the various civil service and offender jobs that were created from the activation of the Health Care Facilities Maintenance program.

In fiscal 2013, the $1.4 million increase in accounts payable and accrued liabilities is primarily attributable to a delay in the State Controller's Office (SCO) processing of CALPIA claim schedules which increased the liability by $1.1 million.

Condensed Statements of Revenues, Expenses and Changes in Net Position

The following table presents the condensed statements of revenues, expenses and changes in net position for the years ended June 30, 2014, 2013 and 2012.

	2014	2013	2012
Operating Revenues	$ 192,642,800	$ 180,246,012	$ 172,669,580
Cost of Goods Sold	146,484,230	141,653,634	143,232,093
Gross Profit	46,158,570	38,592,378	29,437,487
Selling and Administrative Expenses	41,639,600	38,089,843	38,983,323
Operating Income/(Loss)	4,518,970	502,535	(9,545,836)
Non-Operating (Expenses) Revenues, Net	(13,319,234)	(585,630)	688,092
Increase/(Decrease) in Net Position	(8,800,264	(83,095)	(8,857,744)
Net Position at Beginning of Year	95,244,942	95,328,037	104,185,781
Net Position at End of Year	$ 86,444,678	$ 95,244,942	$ 95,328,037

Operating Revenues

As presented in the table above, CALPIA revenue increased $12.4 million (6.9%) to $192.6 million in fiscal 2014 from $180.2 million in fiscal 2013, resulting from increases in service, agriculture, and manufacturing enterprises, of $ 10.9 million (16.2%), $1.0 million (3.7%), and $0.5 million (0.6%) respectively.

In fiscal 2014, the service enterprises had an overall increase in revenue of $10.9 million (16.2%). The increase resulted primarily from the following: an increase in revenue of meat cutting of $1.0 million (9.3%) due to a 13.7% increase in pricing, partially offset by a 4% decrease in volume, an increase in food packaging revenue of $2.7 million (13.5%) based on an increase in packaged lunch and juice sales; increased laundry revenues of $0.7 million (5.0%) based on a higher price per pound, partially offset by a reduction in pounds processed; an increase in printing revenues of $1.3 million (24.4%) due to increased sales to DMV and special print jobs; increased optical revenues of $2.8 million (26.8%) due to an increase in Medi-Cal jobs and increase in construction services and facilities maintenance revenues of $1.8 million (253.8%) based on a new contract with Health Care Facilities Maintenance services.

The increase in agriculture revenue of $1.0 million for fiscal 2014 was primarily the result of an increase in egg production revenue of $1.5 million (25.4%) due to an increase in product sales and revenue per unit based on market price increases. This was offset by a decrease in dairy/farm revenue of $0.2 million (1.3%) due to a decrease in pounds of bulk wholesale milk and sales to CDCR which was offset by overall price increases. Additionally, poultry revenues decreased $0.2 million (3.8%) resulting from a reduction in pounds sold.

The manufacturing enterprises increase in revenue of $0.5 million was primarily the result of an increase of $2.7 million (19.8%) from furniture due to increased chair sales; an increase of $0.6 million (24.6%) from mattress factory due to an increase in product sales primarily due to an increase in sales to CDCR and Coalinga State Hospital, an increase of $1.0 million (16.1%) from cleaning products based on an increase in sales to CDCR. Additionally, in fiscal 2014, CALPIA experienced an increase in manufacturing revenue due to the increased number of projects with California Department of Veteran Affairs (CDVA), California Health Care Facility (CHCF), State Hospitals, and the Department of Military. These projects incorporate new custom products such as the CDVA furniture line. These revenue increases were offset by decreases in fabric products revenue of $2.8 million (12.4%) due to a reduction in highway safety and wildland clothing sales; a decrease in metal products revenue of $0.7 million (7.7%) due to a reduction in cargo body sales, general fabrication of $0.4 million (3.7%) from a decrease in modular system furniture sales offset by increases on non-modular furniture, bindery $0.6 million (27.0%) based on a decrease in placard sales offset by sales of the new retro-reflective road signs, and modular construction $0.09 million (91.1%).

In fiscal 2013, the Service enterprises had an overall increase in revenue of $0.6 million in fiscal 2013. Revenue increased by $3.1 million (18.7%) in food packaging, $0.8 (8.8%) million in meat cutting, $0.3 (10.7%) million in bakery, and $0.7 (404.8%) million in Construction Services Facilities Maintenance. The food packaging revenue increase is attributable to the introduction of pre-packaged lunches in fiscal 2013, increased juice and 4-pack bread sales and additional customers CALPIA was able to retain. The Service enterprise revenue increases were offset by $4.3 million in decreases which were comprised of $2.0 million (13.4%) in laundry due to the reduction in the offender population, $1.2 million (18.9%) decrease in printing due to CDCR's budget reductions and CDCR's ability to make forms available online, an optical decrease $0.5 million (4.1%) due in part to Health Services overpayments from the prior fiscal year that CALPIA paid back during fiscal 2013, as well as a decrease in metal signs of $0.3 million (21.3%) and dental of $0.2 million (27.5%).

Agriculture revenue decreased in total by $0.7 million in fiscal 2013 of which $0.3 million (4.0%) related to poultry, $0.3 million (4.5%) to egg production, and $0.1 million (8.9%) in crops all as a result of the reduction in prison population.

The increase in manufacturing revenue was the result of an increase in sales of metal products, furniture, license plates, fabric products, knitting mill, mattress, bindery, and cleaning products of $13.6 million (23.6%), offset by a decrease in general fabrication revenue of $3.4 million (24.7%) and modular construction of $ 2.0 million (95.5%) in fiscal 2013 due to a reduction in customer demand. Specifically, metal products had a $4.5 million (108.4%) revenue increase in fiscal 2013 primarily due to major projects for the CHCF and Caltrans sales of truck bodies. In furniture, the $3.2 million (31.6%) increase in fiscal 2013 is due to major projects for the CHCF and California Veterans Home. In license plates, the fiscal 2013 increase of $2.4 million (19.0%) is due to California's improved car sales as well as a new program to stock license plate inventory at car dealerships. Fabric revenue increased $2.2 million (11.0%) in fiscal 2013 due to increased sales to California Department of Forestry and Fire Protection (CAL FIRE) and California Department of Transportation (Caltrans) and because CALPIA did not experience a fourth quarter reduction in CPP sales as in fiscal 2012.

	2014	2013	2012
Operating Revenues by Product Line			
Manufacturing:			
Furniture	$ 16,152,647	$ 13,487,601	$ 10,250,388
Metal	8,035,829	8,706,798	4,177,527
License Plates	15,621,115	15,257,567	12,836,502
General Fab.	9,871,023	10,252,030	13,621,163
Bindery	1,547,951	2,120,162	1,887,726
Knitting Mill	1,411,226	1,381,854	1,043,224
Fabric Products	19,512,182	22,285,994	20,056,748
Shoe Factory	4,165,106	3,775,483	4,362,484

Mattress Factory	2,984,957	2,394,996	2,105,064
Cleaning Prod	6,911,586	5,953,468	5,582,873
Modular Construction	8,525	95,775	2,113,820
Total Manufacturing	**$ 86,222,147**	**$ 85,711,728**	**$ 78,037,519**
Services			
Meat Cutting	$ 11,340,089	$ 10,377,158	$ 9,537,937
Bakery	3,297,289	3,310,375	2,989,955
Coffee Roasting	2,009,452	1,900,648	1,863,219
Food & Beverage Packaging	22,388,373	19,723,505	16,617,295
Metal Signs	1,515,430	1,141,915	1,450,890
Printing	6,598,488	5,305,856	6,539,715
Dental Lab	869,503	647,814	894,000
Digital Services	382,280	357,484	310,975
Laundry	13,663,714	13,012,320	15,034,273
Optical	13,329,571	10,514,288	10,965,547
Construction Services & Facilities Maintenance	2,461,055	695,651	137,800
Total Services	**$ 77,855,244**	**$ 66,987,014**	**$ 66,341,606**
Agriculture			
Dairy / Farm	$ 14,040,773	$ 14,220,179	$ 14,313,987
Crops	982,739	1,078,896	1,184,295
Poultry	5,988,656	6,223,872	6,483,583
Egg Production	7,553,242	6,024,323	6,308,590
Total Agriculture	**$ 28,565,410**	**$ 27,547,270**	**$ 28,290,455**
Total Operating Revenues	**$192,642,801**	**$180,246,012**	**$172,669,580**

Cost of Goods Sold

Cost of goods sold increased by $4.8 million (3.4 %) in fiscal 2014 from $ 141.7 million to $146.5 million. Overall, cost of goods sold as a percentage of sales were 76% and 78.6% in fiscal years 2014 and 2013, respectively. Gross profit increased by $7.6 million (19.6 %) from $38.6 million in fiscal 2013 to $46.2 million in fiscal 2014. The increase in gross profit is primarily comprised of a $1.3 million increase in manufacturing enterprises, $6.4 million increase in service enterprises, and offset with a $0.1 million decrease in agricultural enterprises.

In fiscal 2014, the manufacturing enterprises experienced an overall gross profit increase of $1.3 million. This increase primarily resulted from $1.3 million related to cleaning products, $1.2 million to general fabrication, $0.8 million to license plates, $0.7 million to modular construction, $0.6 million to furniture, $.2 million to knitting mill, $.08 million to shoe factory, and $.02 million to mattress. These increases were offset by decreases in metal products of $1.6 million, fabric products of $1.2 million, and bindery of $0.8

million. In an effort to stay current in the manufacturing industry, in fiscal 2014 CALPIA adopted a Lean Manufacturing philosophy within its manufacturing factories. These principles have helped identify areas in the manufacturing process where we could become more efficient and cost effective such as factory layout and just-in-time purchasing. This effort along with the increase in sales has attributed to the increase in gross profit.

Service enterprises had a gross profit increase of $6.4 million in fiscal 2014 from fiscal 2013. The service enterprise increase can be contributed to $2.2 million in optical, $1.3 million in printing, $0.6 million in construction services and facilities maintenance, $0.9 million in food packaging, $0.7 million in meat cutting, $0.5 million in laundry and $0.2 million in coffee roasting. These increases were offset by gross profit decreases of $0.02 million in bakery, $0.05 million in digital services and $0.4 million in construction services. Optical increased in gross profit due to an increase in Healthy Families Medi-Cal program and sharing the work between two factories to meet production demands; printing had an increase in CDCR orders while achieving production efficiencies with new equipment; meat cutting due to an increase in sales from CDCR and refining production processes. In addition, the activation of the Health Care Facilities Maintenance program throughout CDCR contributes the increase in additional revenue of $2.1 million to construction services & facility maintenance.

Agricultural enterprises had a gross profit decrease of $0.1 million which was a combination of a decrease of $0.6 million in dairy, a decrease of $0.1 million in crops, an increase of $0.5 million in egg production, and an increase of $.05 million in poultry. In fiscal 2014, CALPIA made a concerted effort in strategic purchasing of raw materials. Due to the fluctuating nature of service and agricultural commodities, it was imperative for CALPIA's procurement department to follow the markets and make strategic purchases throughout the year. Monitoring these trends in the market and making strategic purchases helped contributed to the reduced COGS and in turn an increase in gross profit margin.

In fiscal 2013, the increase in gross profit is primarily due to increases in revenues due to higher sales demand and the reduction of cost of goods sold. Production was increased to meet the additional sales demands, primarily related to food packaging, metal, furniture, fabric, and license plates. The increase in production enabled fixed overhead costs to be allocated across an increased volume, resulting in improved gross profit margins in various enterprises. In addition, overall cost of goods sold was reduced by making improvements to procurement processes and improving manufacturing efficiencies. Metal raw material costs declined for aluminum resulting in savings in license plates, metal products and metal signs. In addition, there were changes in the procurement method for food raw materials that decreased costs for food products as well as significant reductions in staff for cost savings, consulting services, maintenance and repair, and indirect materials.

Selling and Administrative Expenses

Selling and Administrative expenses are necessary to support CALPIA's daily operations and provide customer service both internally and externally. In fiscal 2014, selling and administrative expenses consisted of distribution and transportation costs of $13.2 million, OPEB expense of $7.4 million, and central office costs of $21.0 million which include all support staff in Central Office divisions. Fiscal 2013, selling and administrative expenses included distribution and transportation costs of $12.5 million, OPEB expense of $7.2 million, and central office costs of $18.4 million.

Non-Operating Expense

Non-Operating expenses increased from $0.6 million in fiscal 2013 to $13.3 million in fiscal 2014 due to the $13.0 million transfer from Prison Industry Revolving Fund to the State of California General Fund.

Product Recall

CALPIA uses an outside consultant to periodically review its product formulations. Subsequent to such a review in July 2012, it was determined that certain fragrance formulations used by CALPIA in its scented bar soap products had been changed by the product supplier and contained an ingredient that has been identified for further study under California's Proposition 65 to determine the maximum level of safe human exposure. As a precautionary measure, on July 27, 2012, CALPIA issued a product recall to its customers for all CALPIA bar-soap products. All CALPIA on-hand inventory was removed from stock and quarantined. In connection with the issuance of its financial statements for fiscal 2012, CALPIA considered the risk and amount of potential loss associated with the inventory recall and determined that its exposure to loss was not material. In fiscal 2013, CALPIA determined that it would not be able to recover its costs associated with inventory and recorded a loss of $1.1 million associated with the recall. While certain lawsuits have been filed against CALPIA and it is unknown if additional filings will occur, CALPIA does not believe that the exposure related to these lawsuits will be material. In fiscal 2014, various lawsuits relating to this matter remain ongoing. CALPIA believes that the ultimate outcome of these lawsuits will not be material to its financial position.

Request for Information

The CALPIA Annual Financial Report is designed to provide a general overview of financial results for fiscal years ended June 30, 2014 and 2013. For questions concerning any information in this report or for additional financial information, contact Michele Kane, Chief of External Affairs, at 916-358-1802 or email Michele.Kane@calpia.ca.gov.

CALIFORNIA PRISON INDUSTRY AUTHORITY

STATEMENTS OF NET POSITION

June 30, 2014 and 2013

ASSETS

CURRENT ASSETS	2014	2013
Cash and cash equivalents	$ 69,674,839	$ 51,293,816
Cash designated for capital assets expenditures	13,959,845	15,425,037
Restricted cash	-	13,000,000
Accounts receivable	5,613,781	3,777,976
Related party receivable	4,500,884	7,692,412
Inventories	37,804,684	40,808,675
Interest receivable	44,698	44,927
Other	281,671	180,628
Total current assets	131,880,402	132,223,471
NONCURRENT ASSETS:		
Capital assets not being depreciated	234,570	1,122,289
Capital assets being depreciated, net	44,903,161	41,861,532
TOTAL ASSETS	$ 177,018,133	$ 175,207,292

LIABILITIES AND NET POSITION

CURRENT LIABILITIES	2014	2013
Accounts payable	$ 11,333,396	$ 9,435,523
Workers' compensation liability-current portion	3,196,782	2,497,999
Unearned revenue	895,972	1,984,609
Accrued expenses and other liabilities	4,150,120	2,852,534
Accrued furlough liability	126,866	126,866
TOTAL CURRENT LIABILITIES	19,703,136	16,897,531
LONG TERM LIABILITIES		
Accrued leave time	9,577,101	10,272,370
Workers' compensation liability	14,485,218	13,343,449
Net OPEB obligation	46,808,000	39,449,000
TOTAL LONG TERM LIABILITIES	70,870,319	63,064,819
TOTAL LIABILITIES	90,573,455	79,962,350
NET POSITION		
Net investment in capital assets	45,137,731	42,983,821
Restricted	-	13,000,000
Unrestricted	41,306,947	39,261,121
TOTAL NET POSITION	86,444,678	95,244,942
TOTAL LIABILITIES AND NET POSITION	$ 177,018,133	$ 175,207,292

See Notes to Basic Financial Statements

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

For the Fiscal Years Ended June 30, 2014 and 2013

	2014	2013
OPERATING REVENUES		
Manufacturing	$ 86,222,146	$ 85,711,728
Services	77,855,244	66,987,014
Agriculture	28,565,410	27,547,270
TOTAL OPERATING REVENUES	192,642,800	180,246,012
COST OF GOODS SOLD	146,484,230	141,653,634
GROSS PROFIT	46,158,570	38,592,378
SELLING AND ADMINISTRATIVE EXPENSES	41,639,600	38,089,843
OPERATING INCOME	4,518,970	502,535
NON-OPERATING REVENUES (EXPENSES)		
Interest income	168,509	209,089
Interest expense	(3,168)	(2,530)
Loss from disposal of capital assets	(344,594)	(678,656)
Transfer to State General Fund	(13,000,000)	-
Other revenue (expenses)	(139,981)	(113,533)
TOTAL NON-OPERATING REVENUES (EXPENSES)	(13,319,234)	(585,630)
Change in net position	(8,800,264)	(83,095)
NET POSITION - BEGINNING OF YEAR	95,244,942	95,328,037
NET POSITION - END OF YEAR	$ 86,444,678	$ 95,244,942

CALIFORNIA PRISON INDUSTRY AUTHORITY

STATEMENTS OF CASH FLOWS

For the Fiscal Years Ended June 30, 2014 and 2013

	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash receipts from customers	$ 192,909,888	$ 177,739,437
Cash receipts from interfund services provided by other funds of the State	2,717,987	657,604
Cash payments for interfund services used by other funds of the State	(10,340,252)	(11,146,341)
Cash payments to employees for services	(54,123,080)	(51,546,210)
Cash payments to suppliers of goods and services	(105,640,352)	(101,649,391)
Transfer to State General Fund	(13,000,000)	-
Cash payments for other services	(139,981)	(113,533)
Net cash provided by operating activities	12,384,210	13,941,566
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Interest expense	(3,168)	(2,530)
Net cash used in noncapital financing activities	(3,168)	(2,530)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisitions of capital assets	(9,219,607)	(6,026,045)
Proceeds from sale of capital assets	585,658	733,811
Net cash used in capital and related financing activities	(8,633,949)	(5,292,234)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest received	168,738	233,522
Net increase in cash and cash equivalents	3,915,831	8,880,324
Cash and cash equivalents at beginning of year	79,718,853	70,838,529
Cash and cash equivalents at end of year	$ 83,634,684	$ 79,718,853

CALIFORNIA PRISON INDUSTRY AUTHORITY

STATEMENTS OF CASH FLOWS (CONTINUED)

For the Fiscal Years Ended June 30, 2014 and 2013

	2014	2013
Reconciliation of operating income to net cash provided by (used in) operating activities:		
Operating income	$ 4,518,970	$ 502,535
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	6,135,445	6,194,851
Transfer to State General Fund	(13,000,000)	-
Other revenue (expenses)	(139,981)	(113,533)
Net effect of changes in:		
Accounts and related party receivables	1,355,723	(2,804,509)
Inventories	3,003,991	885,007
Other assets	(101,043)	79,475
Accounts payable	1,897,873	1,579,024
Unearned revenue	(1,088,637)	297,933
Accrued expenses and other liabilities	1,297,586	(170,217)
Accrued leave time	(695,269)	-
Workers' compensation liability	1,840,552	300,000
Net OPEB obligation	7,359,000	7,191,000
Net cash provided by operating activities	$ 12,384,210	$ 13,941,566

(1) ORGANIZATION

The California Prison Industry Authority ("CALPIA") was established in 1983, as the successor to the California Correctional Industries ("CCI"). It is under the policy direction of an eleven-member board of directors ("Prison Industry Board") and is a component unit of the State of California. CALPIA manages 27 manufacturing, service, and agriculture business lines which includes 73 enterprises/factories that employ offenders at California's penal institutions within the California State Department of Corrections and Rehabilitation ("CDCR"). The CALPIA administrative offices are located in Folsom, California. The products manufactured and services rendered by CALPIA are provided principally to departments of the State of California and other governmental entities.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of accounting - CALPIA uses the accrual basis of accounting. Under this method, revenues and receivables are recorded when earned, and expenses and liabilities are recorded when incurred.

Revenue Recognition - Revenues and receivables are recorded when earned, usually upon the shipment of orders, other than modular furniture and building construction. Revenue on modular furniture and building construction is recognized using a method which materially approximates the percentage-of-completion method of accounting. Under this method, CALPIA recognizes revenue at the end of each period using output measures in terms of results achieved, to measure the extent of progress toward completion under the contract, on the basis of units of work completed.

Cash and cash equivalents - Cash consists of deposits in the custody of the State of California Treasurer. CALPIA's deposits are subject to the California Government Code and the State Treasurer's Office investment policy for the Pooled Money Investment Account ("PMIA"). Cash not required for current use is invested in the Surplus Money Investment Fund ("SMIF"), while non-SMIF funds are held in operating accounts, all of which are part of the State Treasurer's pooled investment program.

These funds are invested through the PMIA and at the direction of the Pooled Money Investment Board, which provides regulatory oversight of such funds. PMIA moneys are limited by State statute to the following investments: U.S. government securities, securities of federally-sponsored agencies, U.S. corporate bonds, interest-bearing time deposits in California banks and savings and loans, prime-rated commercial paper, bankers' acceptances, negotiable certificates of deposits, and other qualifying investments.

The investments in SMIF are reported at amortized cost, which approximates fair value. As of June 30, 2014 and 2013, the weighted average maturity of PMIA investments administered by the State Treasurer's Office was approximately 232 days and 278 days, respectively. Weighted average maturity is the average number of days, given a dollar-weighted value of individual investments, that the securities in the portfolio have remaining from the evaluation date to stated maturity. Neither SMIF nor PMIA are rated by credit rating agencies.

Interest earned on cash invested in the SMIF and other pooled funds are prorated to CALPIA based on its average daily balance.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

At June 30, 2014, $81,598,000 was invested in SMIF and $2,036,684 was held in operating accounts in the State Treasury pooled investment program. At June 30, 2013 $64,041,000 was invested in SMIF and $2,677,853 was held in operating accounts in the State Treasury pooled investment program. Cash and cash equivalents include cash on hand and temporary cash investments (including SMIF, funds designated for capital assets expenditures and restricted cash) with original or remaining maturities of three months or less.

Governmental Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures – An Amendment of GASB No. 3* ("GASB No. 40") requires that governmental entities provide disclosures regarding deposit and investment credit risk, custodial credit risk, interest rate risk, and concentration of credit risk. CALPIA's deposits in the PMIA are not subject to GASB No. 40 risk disclosures except for the disclosures provided above. Additional information regarding investment risks, including interest rate risk, credit risk and concentration of credit risk of the PMIA can be found in the State's basic financial statements included in its Comprehensive Annual Financial Report.

Cash designated for capital assets expenditures - CALPIA segregates its cash which is designated as to use. Designated funds at June 30, 2014 and 2013 represent designations of cash by the Prison Industry Board for certain capital expenditures for the subsequent year. The Board approved funds amounting to $13,959,845 and $15,425,037 for certain capital expenditures to be made during the fiscal years ended June 30, 2015 and 2014, respectively.

Restricted cash - On March 24, 2013, in accordance with California Penal Code Section 2806, at the request of the California Department of Finance, the California State Treasurer's Office directed a transfer of $13 million from CALPIA's Prison Industry Revolving Fund (F0678) to the State of California's General Fund. However, during the fiscal year ended June 30, 2013 the $13 million was transferred by the State Controller from the Prison Industry Revolving Fund to the Prison Industry General Fund because the transfer lacked an appropriation into the State's General Fund. These funds were classified as restricted cash at June 30, 2013 as CALPIA recognized that the funds were not appropriated for operational expenditures. During the fiscal year ended June 30, 2014, the $13 million was transferred to the State of California's General Fund and CALPIA recognized the $13 million transfer as a non-operating expense.

Concentrations of credit risk - Financial instruments which potentially expose CALPIA to concentrations of credit risk consist primarily of trade accounts receivable.

CALPIA's customer base includes departments of the State of California and other governmental entities. CDCR is the largest customer of CALPIA and accounted for approximately 57.1% of sales for the fiscal year ended June 30, 2014 and 57.4% of sales for the fiscal year ended June 30, 2013. As of June 30, 2014 and 2013, CDCR accounted for 47.6% and 67%, respectively, of total accounts receivable. Management does not believe significant credit risk exists at June 2014 and 2013, as the goods and services produced by CALPIA's operations are provided principally to departments of the State of California and other governmental entities.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

CALPIA and other state and local agencies' deposits are held in the pooled money account in the custody of the State Treasurer's Office, in which the deposits are insured by federal depository insurance or by collateral held by an agent of the State Treasurer's Office in the State's name.

Accounts receivable - CALPIA has no formal policy regarding the extension of credit and does not use an allowance for doubtful accounts because their customer base is primarily made up of state and local government agencies. As of June 30, 2014 and 2013, CALPIA has receivables of $443,733 and $445,120, respectively, from non-governmental agencies. Historically, CALPIA has not experienced significant losses related to such accounts receivable.

Due from state general fund - During the course of normal operations, the State Controller's Office periodically loans funds from CALPIA's deposits held in the custody of the State Treasurer to the state general fund on a short-term basis for cash management reasons. These transactions are reported as "due from state general fund." As of June 30, 2014 and 2013, no such amounts were due from state general fund.

Inventories - Inventories are stated at the lower of cost (as determined using the average cost method) or market. Inventories consist of raw materials, components, subassemblies and finished goods held for sale.

Capital assets - Capital assets are stated at historical cost, net of accumulated depreciation. CALPIA has established a threshold of $5,000 for capitalization of depreciable assets. Expenditures for repairs and maintenance are charged to operations as incurred. Depreciation is computed using the straight-line method over the estimated useful lives of the assets. The estimated useful lives range from 5 or 10 years for equipment, 20 years for buildings, 15 years for leasehold improvements, 2 to 3 years for livestock, 20 years for orchards, and 5 years for intangible assets.

Interest expense (net of interest income on unexpended tax-exempt debt proceeds) related to the cost of construction of certain assets is capitalized whenever debt is outstanding and the assets are constructed for use by CALPIA. Capitalized interest is amortized over the related assets' estimated useful lives. CALPIA did not recognize any capitalized interest expense for the fiscal years ended June 30, 2014 and 2013.

In the ordinary course of business, CALPIA opens and closes manufacturing facilities based on economic conditions and industry demand for products. Based on CALPIA's closure policy, management may recommend that the factory remain idle if at a later date it is probable that product demand will increase resulting in the factory being reactivated. If management determines not to reactivate a factory, CALPIA will take one of the following actions: (1) determine if the factory has alternative uses; (2) transfer equipment to operating factories; or (3) pursue other alternatives for disposal. Factories which are closed temporarily are retained in the property accounts as idle facilities and are not depreciated during the temporary closure. At June 30, 2014 and 2013, the net book value of such factories was not material.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Asset impairment - As required by GASB Statement No. 42, management periodically reviews long-lived assets for impairments whenever events or changes in circumstances indicate that the service utility of an asset has declined significantly and unexpectedly.

Impaired capital assets are written down to reduce the related assets to the lower of carrying value or fair value. At June 30, 2014 and 2013, CALPIA determined there were no capital assets impaired.

Compensated absences - It is CALPIA's policy to accrue for personal leave time, holiday pay and vacation pay that has been earned but not yet taken by employees. A liability for compensated absences is accrued when incurred and reported in accrued liabilities on the statements of net position. CALPIA employees are not compensated for unused sick leave, but instead are credited with pension service time for unused sick leave. Accordingly, such convertible sick leave is not reflected in the accrued liability for compensated absences

Unearned revenue - Unearned revenues represent advance payments from customers for the future delivery of products and services.

Net Position - The difference between assets and liabilities in the statements of net position is labeled as Net Position and is subdivided into three categories as follows:

- Net investment in capital assets - This component of net position consists of capital assets, net of accumulated depreciation and amortization.
- Restricted – This component of net position consists of the restricted cash balance.
- Unrestricted - This component of net position consists of amounts not restricted for any project or any other purpose.

Operating and non-operating activities - Operating revenues are charges to customers for sales of products and services. Operating expenses consist of cost of sales and selling and administrative expenses. Selling and administrative expenses are comprised of distribution and transportation costs, central office costs, and the annual OPEB costs. All revenues and expenses not meeting these definitions are reported as non-operating revenues and expenses. Distribution and transportation costs include shipping and handling costs related to the delivery of merchandise sold by CALPIA. For the fiscal years ended June 30, 2014 and 2013, such costs were $13,240,483 and $12,484,710, respectively.

Use of estimates in the preparation of financial statements - The preparation of financial statements in conformity with United States Generally Accepted Accounting Principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

New accounting pronouncements:

In November 2010, the GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus—an amendment of GASB Statements No. 14 and No. 34*. The objective of this Statement is to improve financial reporting for a governmental financial reporting entity. This Statement modifies certain requirements for inclusion of component units in the financial reporting entity. CALPIA adopted this statement for the fiscal year ended June 30, 2013. The effect of the adoption was not material to the financial statements.

In December 2010, the GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements.* The objective of this statement is to incorporate into the GASB's authoritative literature certain accounting and financial reporting guidance found in the following pronouncements issue on or before November 30, 1989:

- Financial Accounting Standards Board Statements and Interpretations,
- The Accounting Principles Board Opinions, and
- The Accounting Research Bulletins of the American Institute of Certified Public Accountants Committee on Accounting Procedure.

CALPIA adopted this statement for the fiscal year ended June 30, 2013. The effect of the adoption was not material to the financial statements.

In June 2010, the GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. GASB Statement No. 63 provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources, introduced and defined in GASB Concepts Statement No. 4. This Statement amends the net asset reporting requirements in Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments,* and other pronouncements by incorporating deferred outflows of resources and deferred inflows of resources into the definitions of the required components of the residual measure and by renaming that measure as net position, rather than net assets. As a component unit of the State of California, CALPIA adopted this statement and applied its requirements to its financial statements for the year ended June 30, 2013. The effect of this adoption was not material to the financial statements.

In March 2012, the GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This Statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. CALPIA adopted this statement for the fiscal year ended June 30, 2014. The effect of the adoption was not material to the financial statements.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

New accounting pronouncements (continued):

In March 2012, the GASB issued Statement No. 66, *Technical Corrections 2012, an amendment of GASB Statements No. 10 and No. 62*. The objective of this Statement is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, and No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. CALPIA adopted this statement for the fiscal year ended June 30, 2014. The effect of the adoption was not material to the financial statements.

In June 2012, the GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions an amendment of GASB Statement No. 27*. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers related to financial support for pensions provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and inter-period equity, and creating additional transparency. As CALPIA participates in the State of California's multi-employer pension system, it is unable to determine the specific impact of this Statement on its net position. However, it believes that the effect is potentially material to its net position. The requirements of this Statement are effective for CALPIA's fiscal year ending June 30, 2015.

In November, 2013, the GASB issued Statement No. 71, *Pension Transition for Contributions made subsequent to the measurement date an amendment of GASB Statement No. 68*. This Statement amends paragraph 137 of Statement 68 to require that, at transition, a government recognize a beginning deferred outflow of resources for its pension contributions, if any, made subsequent to the measurement date of the beginning net pension liability. Statement 68, as amended, continues to require that beginning balances for other deferred outflows of resources and deferred inflows of resources related to pensions be reported at transition only if it is practical to determine all such amounts. The provisions of this Statement are required to be applied simultaneously with the provisions of Statement 68. CALPIA believes that the effect of this Statement is potentially material to its net position. The requirements of this Statement are effective for CALPIA's fiscal year ending June 30, 2015.

(3) INVENTORIES

Inventories consist of the following:

	June 30,	
	2014	2013
Raw materials	$ 20,141,871	$ 24,769,741
Work-in-process	5,271,379	5,629,461
Finished goods	12,391,434	10,409,473
Total inventories	$ 37,804,684	$ 40,808,675

(4) CAPITAL ASSETS

A summary of changes in capital assets during fiscal years 2014 and 2013 is as follows:

	Balance June 30, 2013	Additions	Deletions	Transfers in & out	Balance June 30, 2014
Capital assets, not being depreciated:					
Construction in process	$ 1,122,289	$ 404,216	$ (2,414)	$ (1,289,521)	$ 234,570
Total capital assets, not being depreciated	1,122,289	404,216	(2,414)	(1,289,521)	234,570
Capital assets, being depreciated:					
Equipment	107,140,604	6,533,335	(1,587,895)	42,117	112,128,161
Buildings and leasehold improvements, net of transfers	38,841,817	1,208,765	(146,302)	1,247,404	41,151,684
Livestock	3,704,668	854,381	(991,625)	-	3,567,424
Orchards	874,716	218,910	-	-	1,093,626
Intangible assets	3,671,738	-	-	-	3,671,738
Total capital assets, being depreciated	154,233,543	8,815,391	(2,725,822)	1,289,521	161,612,633
Accumulated depreciation and amortization	(112,372,011)	(6,135,445)	1,797,984	-	(116,709,472)
Total capital assets, being depreciated, net	41,861,532	2,679,946	(927,838)	1,289,521	44,903,161
Capital assets, net	$ 42,983,821	$ 3,084,162	$ (930,252)	$ -	$ 45,137,731

(4) CAPITAL ASSETS (CONTINUED)

	Balance June 30, 2012	Additions	Deletions	Transfers in & out	Balance June 30, 2013
Capital assets, not being depreciated:					
Construction in process	$ 1,233,251	$ 844,773	$ -	$ (955,735)	$ 1,122,289
Total capital assets, not being depreciated	1,233,251	844,773	-	(955,735)	1,122,289
Capital assets, being depreciated:					
Equipment	105,339,902	3,116,545	(1,316,119)	(49,724)	107,140,604
Buildings and leasehold improvements, net of transfers	36,973,613	1,158,013	(295,268)	1,005,459	38,841,817
Livestock	4,312,144	828,994	(1,413,000)	(23,470)	3,704,668
Orchards	874,716	-	-	-	874,716
Intangible assets	3,644,018	27,720	-	-	3,671,738
Total capital assets, being depreciated	151,144,393	5,181,272	(3,024,387)	932,265	154,233,543
Accumulated depreciation and amortization	(107,812,551)	(6,194,850)	1,635,390	-	(112,372,011)
Total capital assets, being Depreciated, net	43,331,842	(1,013,578)	(1,388,997)	932,265	41,861,532
Capital assets, net	$ 44,565,093	$ (168,805)	$ (1,388,997)	$ -	$ 42,983,821

Depreciation expense for the fiscal years ended June 30, 2014 and 2013 was $6,135,445 and $6,194,850, respectively. Depreciation expense includes amortization of intangible assets.

(5) ACCRUED EXPENSES AND OTHER LIABILITIES

	June 30, 2014	June 30, 2013
Accrued leave time	$ 471,197	$ 247,125
Customer deposits	1,210,581	698,301
Support charges due to CDCR	1,109,985	771,398
Inmate pay	321,802	258,623
Personal services	377,055	325,835
Sales and use tax	410,227	229,858
Accrued service and expenses	249,273	321,394
Accrued expenses and other liabilities	$ 4,150,120	$ 2,852,534

(6) ACCRUED FURLOUGH LIABILITY

In February 2009, at the request of the Governor's office, CALPIA and other state agencies instituted involuntary furloughs of substantially all of their employees. The arrangement ceased in October 2010. Unions representing the furloughed employees sued CALPIA and other state agencies seeking repayment of the lost wages. In January 2012 a settlement agreement was reached in which substantially all CALPIA employees would receive reimbursement of all wages withheld during the furlough period, but would waive any right to accrued interest. Two unions representing five CALPIA employees did not consent to the settlement and their civil case remains pending in the Court of Appeals following a judgment entered in the trial court in their favor. At June 30, 2014 and 2013, a reserve of $126,866 has been accrued related to the employees for which a settlement has not been reached.

(7) WORKERS' COMPENSATION LIABILITY

CALPIA is exposed to risk of loss related to torts, theft of, damage to, and destruction of assets, injuries to employees, and natural disasters. The State of California self-insures its workers' compensation claims. CALPIA's workers' compensation claims are administered by the State Compensation Insurance Fund as part of the overall State program. CALPIA currently reports claims, expenses and liabilities when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported and related loss adjustment expenses. Consulting actuaries assist CALPIA in determining its liability for workers' compensation self-insured claims.

The amount of these liabilities was a discounted value of $17,682,000 at June 30, 2014 and $15,841,448 at June 30, 2013. The interest rate used to discount the value of the liabilities as of June 30, 2014 and 2013, was 3.5 percent. This liability represents CALPIA's best estimate of its ultimate exposure based on available actuarial information.

Fiscal Year	Beginning of Fiscal Year Liability	Current Year Claims and Changes in Estimates	Claims Payments	Legal and Administrative Expenses Paid	End of Fiscal Year Liability
2013-2014	$ 15,841,448	$ 5,037,334	$ (2,727,803)	$ (468,979)	$ 17,682,000
2012-2013	$ 15,541,448	$ 2,797,999	$ (2,029,143)	$ (468,856)	$ 15,841,448

(8) DEFINED BENEFIT PENSION PLAN

Plan description - The State is a member of the California Public Employees' Retirement System ("CalPERS"), an agent multiple-employer pension system, which provides a contributory defined benefit pension for substantially all State employees. CALPIA employees are employees of the State. CALPIA is included in the State Industrial and Safety categories within CalPERS, thereby limiting the availability of certain CALPIA pension data. CalPERS functions as an investment and administrative agent for participating public agencies within the State of California. Departments and agencies within the State of California, including CALPIA, are in a cost-sharing arrangement in which all risks and costs are shared proportionately by participating State agencies.

CalPERS issues a publicly available Comprehensive Annual Financial Report that includes financial statements and required supplementary information for CalPERS. A copy of that report may be obtained by logging onto the CalPERS web site at www.calpers.ca.gov/.

The pension plan provides retirement benefits, survivor benefits, and death and disability benefits based upon employee's years of credited service, age and final compensation. Vesting occurs after five years of credited service except for second tier benefits, which require 10 years of credited service. Employees who retire at or after 50 with five or more years of service are entitled to a retirement benefit, payable monthly for the remainder of their lives. Several survivors benefit options, which reduce a retiree's unmodified benefit, are available.

(8) DEFINED BENEFIT PENSION PLAN (CONTINUED)

Funding policy - Active members who participate in Social Security under the State Industrial Tier 1 category are required to contribute 8% to 10% of their annual covered salary after excluding the first $513 of gross monthly pay. Active members who do not participate in Social Security under the State Safety and Industrial Tier 1 categories are required to contribute 9% to 11% of their annual covered salary after excluding the first $317 of gross monthly pay. Effective July 1, 2013, active members who participate in Social Security under the State Industrial Tier 2 category were required to make contributions of 1.5% to CalPERS. Effective July 1, 2014, those active members' required contribution increased to 3.0%.

CALPIA is required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. The actuarial methods and assumptions used are those adopted by the CalPERS Board of Administration. The required employer contribution rate for the fiscal year ended June 30, 2014 was 15.682% and 17.205% for State Industrial and Safety categories, respectively. The required employer contribution rate for the year ended June 30, 2013 was 16.302% and 17.503% for State Industrial and Safety categories, respectively. The contribution requirements of the plan members are established by State statute and the employer contributions rate is established and may be amended by CalPERS.

Annual pension costs - For the fiscal years ended June 30, 2014, 2013 and 2012, CALPIA's annual pension cost and CALPIA's actual contribution amounted to $5,288,396, $5,051,147, and $4,959,793 respectively. The required contribution for State Industrial and Safety categories for the 2014 and 2013 fiscal years were determined as part of the June 30, 2012 and 2011 actuarial valuations using the entry age normal actuarial cost method with the contributions determined as a percent of pay. For the June 30, 2012 actuarial valuation, the actuarial assumptions included (a) 7.50% investment rate of return (net of administrative expenses), (b) projected salary increases that vary by duration of service ranging from 3.20 to 11.20%, (c) 3.00% overall payroll growth, and (d) 2.75% inflation adjustment.

The actuarial value of CALPIA's assets was determined using a technique that smooths the effect of short-term volatility in the market value of investments over a 15 year period. The plan's unfunded actuarial accrued liability (or excess assets) is being amortized as a level of percentage of projected payroll on a closed basis. The remaining amortization periods at June 30, 2013, the date of the most recent actuarial valuation, were 10 to 30 years for the State Industrial Plan and 9 to 30 years for State Safety Plan.

Three-year trend information for CalPERS- State Industrial and Safety Plans:

Fiscal Year Ended June 30	Annual Pension Cost (APC)	Percentage Of APC Contributed	Net Pension Obligation
2014	$ 5,288,396	100%	$ -
2013	$ 5,051,147	100%	$ -
2012	$ 4,959,793	100%	$ -

(9) POSTEMPLOYMENT BENEFITS OTHER THAN PENSION

Plan description - CALPIA employees also participate in the State other postemployment benefit ("OPEB") plan. The State OPEB plan is a single-employer defined benefit plan and the CALPIA participates in the State's plan on a pro-rata cost-sharing basis. A separate actuarial valuation was not performed for CALPIA. The State's OPEB plan does not issue a separate report.

The State provides medical, prescription drug, and dental benefits to retired statewide employees. The authority for establishing and amending benefits lies with CalPERS and the State Legislature, while the authority for establishing and amending the funding policy lies solely with the Legislature.

Funding policy - The State has historically been on a "pay-as-you-go" funding and allocation policy; however, pursuant to the requirements of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, ("GASB No. 45") effective for fiscal year 2008, the State amended its allocation methodology to include amortization of its accumulated unfunded postemployment obligations. The State has determined CALPIA's June 30, 2014 and 2013 funding requirements as well as its related 2014 and 2013 contribution credit. The amount allocated to CALPIA for the years ended June 30, 2014 and 2013 representing the annual OPEB cost was $11,398,000 and $11,056,000 respectively. Of this amount, $4,039,000 was contributed for 2014 and the balance of $7,359,000 was accrued as a liability. The contribution made for 2013 was $3,865,000 and the balance of $7,191,000 was accrued as a liability.

Annual OPEB cost and Net OPEB obligation - The State of California's annual other postemployment benefit cost is calculated based on the annual required contribution of the employer, an amount actuarially determined by the State in accordance with the parameters of GASB No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years. The State determines the allocation for CALPIA based upon the relationship of active employee health benefit costs for CALPIA as compared to the total State active employee health benefit costs. The following table shows the components of CALPIA's allocation of the State's annual OPEB cost for the years, the amount credited to the plan, and changes in the net OPEB obligation as of June 30:

	2014	2013
Annual required contribution	$ 11,199,000	$ 10,898,000
Interest on net OPEB obligation	1,620,000	1,290,000
Adjustment to annual required contribution	(1,421,000)	(1,132,000)
Annual OPEB cost	11,398,000	11,056,000
Contributions made	(4,039,000)	(3,865,000)
Increase in net OPEB obligation	7,359,000	7,191,000
Net OPEB obligation - beginning of year	39,449,000	32,258,000
Net OPEB obligation - end of year	$ 46,808,000	$ 39,449,000

(9) POSTEMPLOYMENT BENEFITS OTHER THAN PENSION (CONTINUED)

CALPIA's allocation of the annual OPEB cost, the percentage of annual OPEB costs contributed to the plan, and the net OPEB obligation for 2014, 2013 and 2012 were as follows:

Fiscal Year Ended June 30,	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
2014	$ 11,398,000	35.4%	$ 46,808,000
2013	$ 11,056,000	35.0%	$ 39,449,000
2012	$ 10,920,000	35.6%	$ 32,258,000

Based on information provided to CALPIA by the State, in the June 30, 2013 actuarial valuation, the individual entry age normal cost method was used. A pay-as-you-go funding scenario was used by the State. Under the pay-as-you-go funding scenario, the State is assumed to finance retiree healthcare benefits from assets available in the general fund. The State's actuarial assumptions included a 4.25% investment rate of return and an annual healthcare cost trend rate of actual increases for 2014 and of 8.50% in 2015, initially, decreasing each year over the next seven years until the ultimate rate of 4.50% is reached. Both rates included a 2.75% annual inflation assumption. Annual wage inflation is assumed to be 3.00%. The unfunded actuarial accrued liability is being amortized as a level percentage of projected payroll on an open basis over thirty years.

The schedule of funding progress and employer contributions for the State of California for the fiscal year ended June 30, 2014 can be found in the State's basic financial statements included in its Comprehensive Annual Financial Report.

(10) RELATED PARTY TRANSACTIONS

Related party transactions with CDCR consisted of the following for the fiscal years ended June 30:

	2014	2013
Assets:		
Accounts receivable	$ 4,500,884	$ 7,692,412
Liabilities:		
Accrued expenses and other liabilities	$ (1,109,985)	$ (868,758)
Unearned revenue	$ (367,551)	$ (367,551)
Revenues:		
Sales	$ 110,006,022	$ 103,368,053
Expenses:		
Support charges paid	$ (4,993,744)	$ (4,304,458)

The secretary of CDCR is the chairman of the Prison Industry Board. Accounts receivable are for the sale of goods and services delivered to CDCR. Accrued expenses and other liabilities represent expenses incurred for rent and utilities associated with the space owned by CDCR and used by CALPIA to operate the offender work programs. Unearned revenue primarily consist of payments received in advance of future delivery of goods and services.

(10) RELATED PARTY TRANSACTIONS (CONTINUED)

CALPIA has transactions with other agencies of the State in addition to CDCR. For the fiscal years ended June 30, 2014 and 2013 sales to such agencies were $77,449,391 and $72,055,585 respectively. As of June 30, 2014 and 2013, CALPIA had accounts receivable from other state agencies of $3,829,004 and $3,041,252 respectively. Additionally, CALPIA received an assessment for statewide administrative costs which were $4,269,451 and $4,788,789 for the fiscal years ended June 30, 2014 and 2013, respectively.

(11) CONTINGENCIES

Under current accounting rules, CALPIA is obligated to record as a liability any difference between its annual pension cost and its annual contribution amount. Historically, CALPIA has covered the fully funded annual pension cost.

In accordance with GASB No. 68, CALPIA anticipates that effective June 30, 2015, it will accrue its actuarially determined unfunded pension obligation. As CALPIA participates in the State of California's multi-employer pension system, it is unable to determine the specific impact on its net position at this time. However, it believes that the effect is potentially material to its net position.

CALPIA is involved in various legal actions arising in the ordinary course of business. In the opinion of management, after consulting with legal counsel, CALPIA intends to defend these cases vigorously and believes that the ultimate liability, if any, will not be material to the financial position of CALPIA.

(12) COMMITMENTS

Warranties - CALPIA provides its customers a warranty period of five years for office furniture and mattress products and ten years for residential hall furniture. CALPIA has not established a reserve for warranty expense as such expenses and liability are deemed to be immaterial by management. Such costs are expensed when incurred.

Rental payments - Future minimum rental payments required under operating leases that have initial or remaining non-cancellable lease terms in excess of one year as of June 30, 2014, are as follows:

Fiscal Year Ended June 30,	Real Estate
2015	$ 378,600
2016	377,328
2017	384,960
2018	392,592
2019	400,229
2020	236,068
Total	$ 2,169,777

Total rental expense for all operating leases was $386,232 and $394,104 for the fiscal years ended June 30, 2014 and 2013, respectively.

SUPPLEMENTAL INFORMATION

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INDEPENDENT AUDITOR'S REPORT
ON SUPPLEMENTAL INFORMATION

To the California Prison Industry Authority Board
Folsom, California

We have audited the basic financial statements of California Prison Industry Authority ("CALPIA") as of and for the years ended June 30, 2014 and 2013, and have issued our report thereon dated November 5, 2014. Our audit was conducted for the purpose of forming an opinion on the basic financial statements as a whole. The supplemental Statements of Net Position, Statements of Revenues, Expenses and Changes in Net Position, and Statements of Cash Flows as of and for the fiscal years ended June 30, 2014 and 2013, classified in accordance with the State Controller's Office Instructions (collectively the "SCO financial statements") are presented for purposes of additional analysis and are not a required part of the basic financial statements. The SCO financial statements are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statements as a whole.

Macias Gini & O'Connell LLP

Sacramento, California
November 5, 2014

CALIFORNIA PRISON INDUSTRY AUTHORITY
INTERNAL SERVICE FUND

STATEMENTS OF NET POSITION
CLASSIFIED IN ACCORDANCE WITH THE STATE CONTROLLER'S INSTRUCTIONS

June 30, 2014 and 2013
(in thousands)

A S S E T S

	2014	2013
CURRENT ASSETS		
Cash and pooled investments	$ 83,635	$ 66,719
Resticted cash	-	13,000
Receivables, (net)	1,825	952
Due from other funds	8,027	10,359
Due from other governments	307	204
Prepaid items	282	181
Inventories, at cost	37,805	40,809
TOTAL CURRENT ASSETS	131,881	132,224
NONCURRENT ASSETS		
Nondepreciable capital assets:		
Construction in process	234	1,122
Depreciable capital assets:		
Buildings	8,235	5,962
Leasehold improvements	32,916	32,880
Equipment	112,128	107,140
Livestock	3,567	3,705
Orchards	1,094	875
Intangible assets	3,672	3,672
TOTAL CAPITAL ASSETS	161,846	155,356
Accumulated depreciation:		
Buildings	(3,873)	(3,554)
Leasehold improvements	(25,502)	(24,526)
Equipment	(82,455)	(79,654)
Livestock	(592)	(457)
Orchards	(793)	(751)
Intangible assets	(3,494)	(3,430)
TOTAL ACCUMULATED DEPRECIATION	(116,709)	(112,372)
TOTAL NONCURRENT ASSETS	45,137	42,984
TOTAL ASSETS	$ 177,018	$ 175,208

L I A B I L I T I E S A N D N ET POSITION

	2014	2013
CURRENT LIABILITIES		
Accounts payable and other	$ 11,333	$ 9,436
Due to other funds	2,247	1,687
Deferred revenue	895	1,985
Other current liabilities	5,228	3,791
TOTAL CURRENT LIABILITIES	19,703	16,899
NONCURRENT LIABILITIES		
Compensated absences payable	9,577	10,272
Net OPEB obligation	46,808	39,449
Other non-current liabilities	14,485	13,343
TOTAL NONCURRENT LIABILITIES	70,870	63,064
TOTAL LIABILITIES	90,573	79,963
NET POSITION		
Net investment in capital assets	45,137	42,984
Restricted	-	13,000
Unrestricted	41,308	39,261
TOTAL NET POSITION	86,445	95,245
TOTAL LIABILITIES AND NET POSITION	$ 177,018	$ 175,208

CALIFORNIA PRISON INDUSTRY AUTHORITY
INTERNAL SERVICE FUND

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION CLASSIFIED IN ACCORDANCE WITH THE STATE CONTROLLER'S INSTRUCTIONS

Years Ended June 30, 2014 and 2013
(in thousands)

OPERATING REVENUES	2014	2013
Services and sales	$ 192,643	$ 180,246
OPERATING EXPENSES		
Personal services	(62,867)	(59,454)
Supplies	(3,525)	(2,187)
Services and charges	(115,596)	(111,908)
Depreciation	(6,135)	(6,195)
Total operating expenses	(188,123)	(179,744)
OPERATING INCOME (LOSS)	4,520	502
NONOPERATING REVENUES (EXPENSES)		
Interest income	168	209
Interest expense	(3)	(2)
Loss on disposal and impairment of of capital assets	(345)	(678)
Other expense	(140)	(114)
Transfer to State General Fund	(13,000)	
Total nonoperating (expenses) revenues	(13,320)	(585)
Change in net position	(8,800)	(83)
NET POSITION AT BEGINNING OF YEAR	95,245	95,328
Net cash provided by operating activities	$ 86,445	$ 95,245

CALIFORNIA PRISON INDUSTRY AUTHORITY
INTERNAL SERVICE FUND

STATEMENTS OF CASH FLOWS
CLASSIFIED IN ACCORDANCE WITH THE STATE
CONTROLLER'S INSTRUCTIONS

Years Ended June 30, 2014 and 2013
(in thousands)

	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from customers	$ 192,910	$ 177,739
Receipts from interfund services provided	2,717	658
Payments for interfund services used	(10,340)	(11,146)
Payments to employees	(54,123)	(51,546)
Payments to suppliers	(105,641)	(101,650)
Payments for other services	(13,139)	(114)
Net cash provided by operating activities	12,384	13,941
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Interest expense	(3)	(2)
Net cash flows used in noncapital financing activities	(3)	(2)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisitions of capital assets	(9,220)	(6,027)
Proceeds from sale of capital assets	586	734
Net cash flows used in capital and related financing activities	(8,634)	(5,293)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest on investments	169	234
Net increase (decrease) in cash and pooled investments	3,916	8,880
Cash and pooled investments, beginning of year	79,719	70,839
Net cash provided by operating activities	$ 83,635	$ 79,719

CALIFORNIA PRISON INDUSTRY AUTHORITY
INTERNAL SERVICE FUND

STATEMENTS OF CASH FLOWS
CLASSIFIED IN ACCORDANCE WITH THE STATE
CONTROLLER'S INSTRUCTIONS

Years Ended June 30, 2014 and 2013
(in thousands)

RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES	**2014**	**2013**
Operating income	$ 4,520	$ 502
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	6,135	6,195
Other fees	(13,140)	(114)
Net effect of changes in:		
Receivables	(873)	(208)
Due from other funds	2,332	(2,623)
Due from other governments	(103)	27
Prepaid items	(101)	79
Inventories	3,004	885
Accounts payable and other	1,897	1,580
Due to other funds	560	(729)
Deferred revenue	(1,090)	298
Other current liabilities	1,437	882
Compensated absenses payable	(695)	246
Other liabilities	8,501	6,921
Total adjustments	7,864	13,439
Net cash provided by operating activities	$ 12,384	$ 13,941

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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the California Prison Industry Authority Board
Folsom, California

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the California Prison Industry Authority (CALPIA), an component unit of the State of California, as of and for the fiscal years ended June 30, 2014 and 2013, and the related notes to the financial statements, which collectively comprise CALPIA's basic financial statements, and have issued our report thereon dated November 5, 2014.

Internal Control over Financial Reporting

In planning and performing our audits of the financial statements, we considered CALPIA's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of CALPIA's internal control. Accordingly, we do not express an opinion on the effectiveness of CALPIA's internal control.

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether CalPIA's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. 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 disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Macias Gini & O'Connell LLP

Sacramento, California
November 5, 2014