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Great Plains Region

Audit Report

Food and Nutrition Service
National School Lunch Program
Cost-Reimbursable Contracts with a
Food Service Management Company

Report No. 27601-15-KC
December 2005

UNITED STATES DEPARTMENT OF AGRICULTURE

OFFICE OF INSPECTOR GENERAL

Washington D.C. 20250

DEC 09 2005

REPLY TO
ATTN OF: 27601-15-KC

TO: Roberto Salazar
Administrator
Food and Nutrition Service

ATTN: Lael Lubing
Director, Grants Management Division

FROM: Robert W. Young /s/
Assistant Inspector General
for Audit

SUBJECT: National School Lunch Program – Cost-Reimbursable Contracts with a Food Service Management Company

This report presents the results of our audit of cost-reimbursable contracts between school food authorities (SFA) and a food service management company (FSMC). Your October 29, 2005, response to the draft report is included as exhibit F with excerpts and the Office of Inspector General's position incorporated into the relevant sections of the report. Your reply generally expressed agreement with the recommendations, but provided insufficient information to reach management decisions for them. The Findings and Recommendations section of the report explains those actions necessary for us to consider management decisions on Recommendations 1 and 2. In general, we will need to be advised of the specific actions completed or planned along with acceptable dates for completing the proposed actions in order to consider the management decisions for them.

We expanded exhibit D in response to earlier Food and Nutrition Service (FNS) comments that it did not provide enough information to understand the relationships between the FSMC, its suppliers, its food service sector, and the SFA. We believe that the current exhibit D reasonably depicts these complex relationships. In response to your comments about the use of regulatory citations, we have changed the citations to "Federal regulations" in order to be consistent.

In accordance with Departmental Regulation 1720-1, please furnish a reply within 60 days describing corrective actions taken or planned and the timeframes for accomplishing final action. Please note that the regulation requires management decisions to be reached on all findings and recommendations within 6 months from the date of report issuance.

We appreciate the assistance provided to us during the review.

Executive Summary

National School Lunch Program – Cost-Reimbursable Contracts with a Food Service Management Company (Audit Report No. 27601-15-KC)

Results in Brief

A Food Service Management Company (FSMC) is a commercial enterprise or a nonprofit organization, which is or may be contracted with by a school food authority (SFA) to manage any aspect of the school food service to include purchasing food products on behalf of the SFA and subsequently billing the SFA for the purchases. We initiated this audit to determine whether the FSMC passed on cost savings on food purchases to SFAs when required to do so by contract. We also conducted the audit to obtain information for the Food and Nutrition Service (FNS) to consider when developing their policies or procedures on the treatment of purchase incentives.

In 106 contracts with SFAs, our audit determined that the corporation did not pass on at least $1.3 million in savings it received although the 106 contracts specifically required the crediting back of the funds. The savings came from incentives, discounts, rebates, etc., that the FSMC negotiated from food manufacturers.[1] Although these manufacturers did not sell directly to the FSMC, they did sell to distributors from which the corporation bought food for the SFAs. The SFAs then reimbursed the school food service sector of the corporation for the amounts it had bought from the distributors. This price did not reflect the incentives received earlier up the supply chain from the manufacturers.

In June 2002, we discussed the issue with FSMC officials. They agreed that manufacturers had given the corporation incentives that it kept rather than crediting them back to the SFAs. Figures they provided indicated that the FSMC retained over $6 million in incentives between September 1998 and December 2001. In response to our question as to whether they had credited any of the $6 million in incentives to the SFAs, company officials stated that none of the incentives were credited back to the SFAs. We were unable to determine how much of this amount beyond the $1.3 million above would have gone to the 106 SFAs, per the contracts, because the company's accounting system did not break out cost allowances to individual SFAs (see finding 1).

[1] For the purpose of this report, FSMC is used to apply to both the parent corporation and its school food service sector. The parent corporation generally contracted with food manufacturers and distributors while its school food service sector contracted to be the FSMC for individual school districts. In addition, the local, regional, and national volume allowances, rebates, credits, discounts, cash prompt payment discounts, signing bonuses, administrative fees, and other volume purchase incentives, are considered to be one and the same.

At a later meeting in August 2002, FSMC officials asserted that SFAs received lower prices overall because of the corporation keeping the purchase incentives. In addition, they stated that the FSMC was subsidizing its administrative fees by keeping the purchase incentives. To verify their assertion concerning the lower prices, we compared invoices from a distributor (the FSMC's basis for billing the SFA) to the FSMC and invoices from the same distributor to a second FSMC customer for the same 2 months. We found that for 35 identical items, the FSMC paid between $0.19 and $13.31 more per item for 29 items than the second FSMC. The second FSMC paid between $0.02 and $0.76 more per item for six items than the FSMC. In other words, in addition to not receiving incentives, SFAs were likely paying more with the FSMC.

In addition, we obtained an SFA's comparison of FSMC responses to its request for proposal, which stated that cost accounted for 20 of 100 maximum points in evaluating the proposal. We added the purchase incentives the FSMC received for purchases for this SFA for the school year ended June 30, 2001, to the management fees. We determined that with the purchase incentives added to the FSMC's management fee, its total projected costs exceeded that of the other FSMC bidders. We found no indication that the SFA officials knew at the time of contract award that the FSMC was planning to obtain and keep purchase incentives on purchases made on behalf of the district.

When we requested documents to support one SFA's reimbursements paid to the FSMC, a manager with its school food service sector provided invoices the company received from the distributors, which did not reflect the incentives received from manufacturers. In addition, the State agencies responsible for overseeing the SFAs' contracts did not have procedures in place to ensure that the SFAs included and enforced the incentive provisions. Most of the State agencies stated that the SFAs were responsible for ensuring that the contracted FSMCs complied with contract requirements.

Federal regulations require "a contract administration system which ensures that contractors perform in accordance with the terms, conditions, and specifications of their contracts or purchase orders."[2] FNS noted that current Federal regulations provide that the parties to the contract (i.e. SFA and FSMC) are responsible for ensuring the enforcement of the terms and conditions of the contract. FNS has proposed Federal regulations[3] to clarify that State agencies must check

[2] 7 Code of Federal Regulations (CFR) 3016.36(b)(2). (Regulations in 7 CFR 3016 apply USDA-wide while regulations in 7 CFR 210 apply solely to FNS programs.)
[3] Federal Register Volume 69, Number 250, page 78340 dated December 30, 2004, to amend 7 CFR 210, 215, and 220.

SFA contracts for compliance on a yearly basis. The proposed Federal regulations also require that companies providing cost reimbursement food management services identify all discounts, rebates, and other applicable credits when billing an SFA.

Recommendations In Brief

We recommended that FNS reinforce that the State agencies need to instruct the SFAs to take action to enforce the contract terms and recover incentives due to the SFAs' food service accounts.

Agency Response

The agency response showed general agreement with the audit conclusions with the exception of the treatment of prompt payment discounts. FNS stated it only prohibits the retention of earned income or prompt payment discounts earned by the FSMC when the amounts are earned using funds advanced by the SFA. We incorporated their comments in the applicable sections of the report and attached a copy of the comments as exhibit F.

OIG Position

We continue to believe that the costs billed by the company to its SFAs with cost-reimbursable contracts should be the net costs incurred by the company for food, beverages, and supplies purchased on behalf of the SFA's nonprofit food service. The prompt payment discounts are a reduction in the costs incurred by the company for the purchased items. These amounts should be treated no differently than any other volume purchase incentive unless stipulated by contract terms. While the majority of the 106 contracts contained a general requirement that "discounts" should be credited to the SFA, a contract that did specifically mention prompt payment discounts provided that these discounts should also be credited to the SFA. In the absence of specific contract terms, we believe deference needs to be given so that these amounts accrue for the benefit of the SFAs. Lastly, we are concerned that allowing the company to keep one type of discount will lead to the labeling of all discounts and rebates as the type of discount that the company is allowed to keep and continuation of the current practices by retaining discounts and understating the cost of management fees or other costs in contract proposals may inhibit competition among FSMCs.

Abbreviations Used in This Report

CFR	Code of Federal Regulations
FNS	Food and Nutrition Service
FSMC	Food Service Management Company
FY	Fiscal Year
IFB	Invitation for Bid
NSLP	National School Lunch Program
OGC	Office of the General Counsel
OIG	Office of Inspector General
OMB	Office of Management and Budget
RFP	Request for Proposal
SBP	School Breakfast Program
SFA	School Food Authority
USDA	U.S. Department of Agriculture

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Background and Objectives

Background

Food and Nutrition Service (FNS), an agency of the U.S. Department of Agriculture (USDA), administers the National School Lunch Program (NSLP) and the School Breakfast Program (SBP). FNS enters into written agreements with a State agency, usually a State's Educational Agency, which administers the program Statewide. The State agency is required to perform program oversight through monitoring and assisting School Food Authorities (SFAs) in their operation of the NSLP/SBP at the local level.

Federal regulations permit SFAs to contract with Food Service Management Companies (FSMCs) to manage their food service operations. Although management companies can provide most of the routine administration of the food service operations, the SFA retains the responsibility of ensuring that food operations comply with Federal regulations.

An SFA solicits bids from management companies through issuing either a request for proposal (RFP) or invitation for bid (IFB) that details the contract requirements. In a cost-reimbursable contract, management companies can make purchases on behalf of the SFA and submit the invoices to the SFA for payment. FNS guidance provides that these contracts should require that certain types of benefits accrue back to the SFA. Under a cost-reimbursable contract, any discounts and rebates the management companies may receive that would reduce the cost of goods purchased should be passed along to the SFAs, as these represent a reduction in the actual costs involved in preparing the meals.

State agencies have certain monitoring responsibilities. Federal regulations[4] require State agencies to review each contract between an SFA and an FSMC annually to ensure compliance with Federal requirements. The State agency is required to perform an onsite review of each SFA contracting with an FSMC at least once during each 5-year period. Such reviews shall include an assessment of the SFA's compliance with Federal regulations covering SFA contracts with FSMCs.

The State agency is encouraged to conduct such a review when performing Coordinated Review Effort reviews, which are onsite

[4] 7 Code of Federal Regulations (CFR) 210.19(a)(6).

administrative reviews the State agency is required to perform at each SFA at least once during each 5-year period.[5]

Federal regulations[6] allow local governments operating USDA entitlement programs to use their own procurement procedures that reflect applicable State and local laws and regulations, as long as those procedures are consistent with the requirements found in 7 CFR 3016.36(b) through (i) and 3016.60(b) through (c). These Federal regulations state that costs or prices based on estimated costs for contracts under grants are allowable only to the extent that costs incurred or cost estimates, included in negotiated prices, are consistent with Federal cost principles referred to in Federal regulations.[7] These Federal regulations state that Federal cost principles applicable to State and local governments are located in Office of Management and Budget (OMB), Circular A-87, Cost Principles for State and Local Governments. OMB Circular A-87, in Attachment A, Section C, paragraphs 1i and 4a, stipulates that to be allowable, a cost must be the net of all applicable credits, such as purchase discounts, rebates, or allowances. FNS' interpretation and position were that the cost principles of OMB Circular A-87 applied to contracts entered into by SFAs, or their agents, and contractors. Since FNS believed that the OMB Circular A-87 cost principles were applicable to contracts between SFAs and FSMCs, it had not codified this requirement in Federal regulations.

In a previous audit report, we reported that of 19 SFAs reviewed nationwide with cost-reimbursable contracts, 7 did not receive credit for the discounts and rebates their two management companies received on purchases.[8] We attributed this to a lack of mandated specific contractual terms relating to discounts and rebates, which enabled the FSMCs to use contract terms that allowed them to retain the discounts and rebates. In addition, we reported that FNS had not issued clear monitoring procedures in Federal regulations for State agencies to follow in determining exactly how an FSMC should pass through the value of discounts and rebates. FNS advised that OMB's position is that FNS cannot mandate specific language in a contract between the FSMC and the SFA. This is why FNS has proposed Federal regulations that focus on defining allowable costs in the program.

The previous report recommended FNS:

[5] 7 CFR 210.18 (b)(1) and (2), and (c)(1).
[6] Final rule, effective August 14, 2000, for 7 CFR 3015, 3016, and 3019.
[7] 7 CFR 3016.22.
[8] Audit 27601-27-CH, "NSLP – Food Service Management Companies," issued April 30, 2002.

(1) Amend its Guidance for School Food Authorities to identify specific contract terms that a State agency and SFA must use to ensure that FSMCs comply with all applicable competitive procurement procedures that should result in net costs being charged to an SFA so that the SFA, and not the FSMC, receives the benefit of cost reductions in the form of discounts, rebates, and allowances;

(2) Amend Federal regulations to require that State agencies include language in their RFP prototypes that require contract review by State officials prior to the SFA signing and implementing a management company contract;

(3) Amend Federal regulations and Guidance for State Agencies to require each State agency to annually review and approve each contract between any SFA and management company to ensure compliance with all the provisions and standards set forth in 7 CFR 210.16, before contract execution; and

(4) Notify all FNS regional offices to inform their State agencies that all new contracts must require that only costs net of all discounts or rebates are allowable costs to be charged to the SFA's nonprofit food service account and that any current contracts that do not contain this requirement must be rebid as soon as possible.

In its replies to our recommendations, FNS agreed to amend and reissue revised guidance for SFAs to help ensure that FSMCs comply with competitive procurement procedures that should result in net costs being charged to an SFA and contracts were to require that only costs net of all discounts or rebates were allowable. FNS later obtained our agreement to change their management decisions on amending the guidance to "pursuing regulatory action to ensure that SFA contracts contain provisions requiring FSMCs to charge only allowable costs that are net of credits, discounts, and rebates." These recommendations are still awaiting final action.

During the first quarter of Fiscal Year (FY) 2003, FNS received an interpretation from OMB regarding the applicability of the requirements of OMB Circular A-87 to the contracting activities between SFAs and FSMCs. OMB personnel verbally told FNS and the Office of the General Counsel (OGC) that they believed Circular A-87 provisions did not apply to the contracts between SFAs and FSMCs and the existing Federal regulations (alone) could not govern the FSMC's actions (or similar third parties) without the specific requirements being stated in the contract's language. In order to enforce compliance, FNS would need to codify in Federal regulations

that costs charged to SFAs must be allowable and net of any discounts, rebates, and other allowances.

FNS distributed a memorandum,[9] which stated its position on the crediting of discounts and rebates in cost-reimbursable contracts remained unchanged. FNS stated that it strongly encourages, but does not require, that all cost-reimbursable contracts include provisions to ensure SFAs are only charged net, allowable costs. FNS further stated that OMB and OGC have made it clear that State agencies and SFAs can impose compliance with net cost requirements through contractual terms. FNS has proposed a change to Federal regulations to prohibit SFAs from using funds in the nonprofit school food service account for expenditures made under any cost-reimbursable provisions of a contract that permits the contractor to receive payments in excess of the contractor's actual net allowable costs. Such net allowable costs must include, but are not limited to, discounts and rebates to the contractor.

During fieldwork for two related audits,[10] we became aware that the FSMC was receiving discounts and rebates on purchases made for the school food service programs of its contracted SFAs in Missouri. In discussions with FNS Headquarters officials, it was determined that we would conduct an audit of contracts between the FSMC and its SFAs to establish the number of contracts that specified that applicable purchase incentives be passed through to the SFAs and whether the FSMC was in compliance with these contract provisions.

The FSMC reported it was the world's largest food service company and had FY 2003 revenues of $6 billion throughout the United States and Canada. In 2004, the FSMC reported providing food service to over 500 school districts in the United States, serving over 1.5 million meals daily.

Objectives

Our objective was to determine whether the FSMC passed on cost savings to SFAs for whom it had contracted to purchase food, and to obtain information for FNS to consider when developing their policies or procedures on the treatment of purchase incentives.

[9] A July 9, 2004, memorandum addressed to all Regional Directors, Child Nutrition Programs.

[10] Audit 27601-13-KC, dated March 2002, and Audit 27601-14-KC, Food Service Management Company Cost Reimbursable Contracts in Missouri, dated December 2002.

Findings and Recommendations

Section 1. Contract Compliance

Finding 1 Contract Provisions Were Not Enforced

SFAs did not enforce contract provisions that required the FSMC to deduct incentives it received when purchasing food for SFAs from the price it charged for that service.[11] Generally, the State agencies charged with overseeing the SFAs indicated that the SFAs themselves were responsible for enforcing the terms of their contracts. There were no procedures in place, however, to monitor whether or not the SFAs were doing so for any of the 22 State agencies we examined. As a result, where contract language did specify a return of incentives to the local SFA, 106 SFAs across 8 States paid the FSMC at least $1.3 million more than called for by their contracts.

Federal regulations generally require grantees and subgrantees to maintain a contract administration system that ensures that contractors perform in accordance with the terms of their contracts.[12] Although there are general oversight requirements, no specific Federal regulation, however, directed either State agencies or SFAs to monitor their contracts for compliance. While Federal regulations in 7 CFR 210 only permit SFAs to use nonprofit school food service account funds for allowable costs, current Federal regulations do not define the nature, terms, or conditions of the language related to allowable costs that should have been included in the contract between the SFA and the FSMC. FNS has published a proposed Federal regulation[13] that would require solicitation and contract documents include specific terms and conditions. The proposed Federal regulation would require State agencies, on a yearly basis, to review FSMC contracts before the execution of the contract by the SFA and FSMC.

At our behest, the FSMC provided data that showed it received over $6 million in incentives on purchases made for 298 SFAs in 22 States between September 1998 and December 2001. During meetings and other communications, company officials stated that none of the $6 million was passed on to the SFAs. See exhibit D for a flowchart showing the flow of money and food to and from the parent corporation, its school food service sector, its vendors and distributors,

[11] In addition, the local, regional, and national volume allowances, rebates, credits, discounts, cash prompt payment discounts, signing bonuses, administrative fees, and other volume purchase incentives, are considered to be one and the same.
[12] 7 CFR 3016.36(b)(2), January 1, 2001, edition.
[13] Federal Register Volume 69, Number 250, page 78340 dated December 30, 2004.

and school districts. Although 142 of the contracts did not have provisions that required the corporation to pass on incentives,[14] the remaining 106 did.

Seven State agencies did not provide us with SFA contracts in place during the audit scope (FY 1998-2002) for the remaining 50 SFAs. Generally, the agencies advised us that they had not kept the contract documents for the required retention period, or had disposed of documents still in effect once a contract was extended. Federal regulations require State agencies to retain their records for a period of 3 years after final claims and reports for a given FY.[15]

We were able to break down most, but not all, of the $6 million in incentives to purchases made on behalf of particular SFAs. The FSMC's accounting system recorded all of the cash discounts it had received for the scope of our audit (FY 1998-2002). The system maintained the total volume allowances (incentives given for buying a certain quantity), but only broke down the figures for individual SFAs for FYs 2001 and 2002. Even those 2 years, however, did not include local rebates and national distributor allowances.

From our review of the company's accounting records, we were able to break out the $6 million in the following manner: $1.3 million in incentives for purchases made on behalf of 106 SFAs with contracts that required incentives to be passed on to the schools; $1.8 million in incentives for SFAs that did not have contracts requiring the firm to pass on the incentives; $600,000 in incentives for the 50 SFAs where copies of the contract could not be obtained; and $2.3 million in incentives that could not be attributed to any SFA due to a lack of documentation in the company's accounting records.

During a conference with FSMC officials on August 6, 2002, they asserted that all SFAs received lower overall prices because the corporation kept the incentives. In addition, they stated that the company was subsidizing (lowering) its administrative fees charged to the SFAs by keeping the purchase incentives. To verify their assertion concerning the lower prices, we compared invoices from a distributor (the FSMC's basis for billing the SFA) to the FSMC and invoices from the same distributor to a second FSMC customer for the same 2 months. We found that for 35 identical items,[16] the FSMC paid

[14] We noted that 7 of the 142 contracts required the SFAs to select a food vendor but they did not. Instead, they allowed the FSMC to choose the vendor with the effect that incentives that might have accrued to the SFA went to the FSMC.
[15] 7 CFR 210.23(c).
[16] In order to ensure the items were identical, emphasis was placed on identifying items with the same vendor number and brand name ordered by both FSMCs.

between $0.19 and $13.31 more per item for 29 items than the second FSMC. The second FSMC paid between $0.02 and $0.76 more per item for six items than the FSMC. Therefore, contrary to the FSMC's assertion, based on our analysis, SFAs were more likely than not to be paying more with the FSMC than with the second FSMC, even though the FSMC kept all the incentives. Accordingly, we conclude little creditability in the FSMC's assertion to us.

In addition, the treatment of incentives could have affected the outcome of contract awards. We obtained an SFA's comparison of FSMC responses to its request for proposal, which stated that cost accounted for 20 of 100 maximum points in evaluating the proposal. We analyzed the amount of purchase incentives the FSMC received for purchases for this SFA in the school year ended June 30, 2001, along with the management fees received. We determined that with the purchase incentives considered along with the FSMC's charges for management fees, these total costs exceeded that of the other FSMC bidders. We found no indication that the SFA officials knew at the time of contract award that the FSMC was planning to obtain and keep purchase incentives on purchases made on behalf of the district. However, the retention of these incentives enabled the FSMC to offer lower costs, management fees, etc., than it would have been able to had it been required to give incentives to the SFAs.

Because we have already provided recommendations in the prior report to improve controls and amend Federal regulations, we are not offering any further recommendations in these areas in this report.

Recommendation 1

Direct the State agencies to provide oversight to ensure the applicable SFAs take action to enforce the contract terms and recover the purchase incentives due to the SFAs' food service account.

FNS Response.

On October 29, 2005, FNS wrote that they agreed with our conclusions in a number of areas within the report and would be working to implement corrective action for the problems noted. However, FNS disagreed with the Office of Inspector General's (OIG) treatment of prompt payment discounts. FNS noted that OIG refers to these payments as examples of volume purchase incentives that the FSMC is not entitled to receive either by contract stipulation between the SFA and the FSMC or by Federal policy. While OIG is correct in stating that the contract between the SFA and FSMC will control the disposition of such amounts, in the absence of specific contract terms,

Agency policy only prohibits the retention of earned income or prompt payment discounts earned by the FSMC when the amounts are earned using funds advanced by the SFA.

In addressing OIG's findings, we will direct State agencies to work with their SFAs to evaluate FSMC contract compliance pursuant to the terms of those contracts. As in any similar situation, when unallowable nonprofit school food service account expenditures are identified, one element of the accepted corrective action is the restoration of these amounts to the affected nonprofit school food service accounts. However, we cannot require that State agencies direct SFAs to restore funds to the nonprofit school food service accounts for expenditures that are otherwise allowable.

OIG Position.

We continue to believe that the costs billed by the company to its SFAs with cost-reimbursable contracts should be the net costs incurred by the company for food, beverages, and supplies purchased on behalf of the SFA's nonprofit food service. The prompt payment discounts are a reduction in the costs incurred by the company for the purchased items and should be treated no differently than any other volume purchase incentive unless specified by contract terms. This includes where purchases for school food service accounts are unique and/or represent a preponderance of the purchases made by the FSMC. The majority of the 106 contracts stated only that "discounts" should be credited to the SFA and did not differentiate between prompt payment and sales discounts. In addition, one contract that did specifically mention prompt payment discounts stated that these discounts should also be credited to the SFA. Lastly, we are concerned that allowing the company to keep one type of discount will lead to the labeling of all discounts and rebates as the type of discount that the company is allowed to keep. In our view, deference should be given so that the term "discounts" as used in these contracts is all-inclusive.

The FNS response stated that its Agency policy only prohibits the retention of earned income or prompt payment discounts earned by the FSMC when the amounts are earned using funds advanced by the SFA. In their earlier correspondence on this subject, FNS provided three non-USDA documents[17] as support for their policy regarding the prompt payment discounts. However, FNS provided no written USDA

[17] Decision of the Comptroller General in the matter of Lankford-Sysco Food services, Inc.; Sysco Food Services of Arizona, Inc., dated January 6, 1997; Decision of the Comptroller General in the matter of Government Printing Office - Treatment of Prompt Payment Discounts dated August 28, 1998; and U.S. Department of Health and Human Services, Departmental Appeals Board Decision No. 400, March 29, 1983, Maryland Department of Health and Mental Hygiene.

directives or OGC decisions to support this policy; FNS could not provide evidence that it ever distributed this policy in formal written correspondence internally or externally to State agencies and SFAs. Our position remains unchanged that the terms of the written contracts should control the disposition of these amounts. Accordingly, these amounts should be restored to nonprofit food service accounts where contract terms stipulate their unallowability. In order to consider the management decision for this recommendation, we need to be informed of the specific actions FNS plans to direct the States to take and timeframes to accomplish them.

Recommendation 2

In accordance with Federal regulations,[18] instruct the 7 State agencies that did not retain the 50 SFA contracts to develop and implement those procedures necessary to ensure original contracts with FSMCs are retained for as long as they are effective, including the time covered by any extensions and/or renewals.

FNS Response.

On October 29, 2005, FNS wrote that they agreed with the auditors' conclusions in a number of areas within the report and would be working to implement corrective action for the problems noted.

OIG Position.

In order to achieve a management decision for Recommendation 2, we need to be informed of the corrective actions taken or planned, and the timeframes for implementation of the corrective action.

[18] 7 CFR 210.23(c).

General Comments

During our review, we observed other conditions regarding reimbursements for "a la carte" meals (separate prices for each item on a menu) that merit consideration by FNS. It is the policy of FNS to encourage the service of reimbursable meals. Two State agencies did not have policies and procedures to prevent SFAs from accepting questionable contract clauses that encouraged consumption of "a la carte" meals rather than reimbursable program meals. To be reimbursable under the NSLP/SBP, a meal served to an eligible child must meet minimum nutritional standards and be priced as a unit.[19] In the FSMC contracts we reviewed, the contracts provided a meal equivalency rate that was used to convert "a la carte" and other nonreimbursable sales (adults, catering, etc.) into meal equivalents. The contracts also provided factors for converting reimbursable breakfasts and snacks into meal equivalents. The standard conversion factors were two breakfasts or three snacks equal one meal equivalent. According to the contract provisions, the FSMCs earned their administrative and management fees based on the number of reimbursable meals and meal equivalents provided. In the contracts reviewed, these fees were to be increased when the FSMC reached certain targets that included meal equivalents. Incentive fees that are based on the service of meal equivalents that are calculated at less than the free meal reimbursement rate plus the value of entitlement donated foods reward the service of "a la carte" meals, not reimbursable meals, which does not support FNS' policy.

- In one State, an SFA signed a food service contract that included an incentive clause that provided escalating management fees to a third FSMC for ranges of increases in meals served, including meal equivalents for "a la carte" meals. A State agency official stated a belief that the State agency did not have the authority to question the SFA's judgment. In essence, the SFA paid additional management fees to encourage meals not meeting program requirements.

  This SFA's contract obtained the number of meal equivalents by dividing the total of its gross sales, including cash for adult meals, "a la carte" meals, milk, snack bar, catering, conferences, and other functions sales (excluding reimbursable lunches,) by $2. This meal equivalency rate was less than the

[19] 7 CFR 210.2, 210.10(a), and 7 CFR 220.7(e)(3).

free meal reimbursement rate plus the per meal entitlement rate for donated foods.

- Five SFAs in another State signed contracts with the first FSMC that contained provisions for increased fees after reaching a specified level for meals and meal equivalents. For example, the contract between one of the five SFAs and the FSMC for the school year ended in 2002, provided that the FSMC shall invoice the SFA for a per-meal charge for all meal and meal equivalents based upon the following scale for the management fee: $0.0199 for 0 to 1,400,000 meals, and $0.0599 for 1,400,001 and above meals. This contract clause resulted in the SFA paying an additional $14,977 in management fees during the school year ended in 2002. The availability of the higher management fee for meal equivalents provided an incentive to the FSMC to serve "a la carte" menu items rather than reimbursable meals.

  The contract for the previously mentioned SFA states that for management fee purposes, the number of meal equivalents shall be determined by dividing the total of all sales, by the student charge for a fully paid lunch at each level. Catering equivalents would use the Middle School student charge. The lunch charges were identified as follows: High School: $2.35, Middle School: $2.00, and Elementary School: $1.65. The total of all sales used in the calculation of meal equivalents would include cash for adult meals, "a la carte" meals, milk, snack bar, catering, conference, and/or any other function sales (excluding reimbursable meals). The free lunch reimbursement plus the value of entitlement donated foods for this same period was $2.245.

Scope and Methodology

We initiated our audit by using the documents obtained from the FSMC to determine the amount of volume purchase allowances and cash discounts it reported as received on NSLP/SBP purchases for its contracted SFAs during the period July 1, 1998, through December 31, 2001.

- We obtained information about the amount and scope of discounts received by it and/or its subsidiary nationwide. The company provided documents that primarily included contracts, pricing sheets, discounts, and volume allowances received, broken down by SFAs as cost centers and correspondence between the company and its distributors and suppliers.

- We also reviewed the documents obtained from the FSMC's headquarters to identify contracts between it and its school food service sector and distributors and vendors, such as food manufacturers.

- After identifying the contracts, we reviewed them for contract terms that provided for the FSMC to receive cash discounts, volume allowances, and other purchase incentives for purchases relating to the NSLP/SBP.

We also used information from a distributor for the FSMC and a second FSMC customer and compared prices charged for food and supplies to SFAs contracted with the FSMC's school food service sector and SFAs contracted with the second FSMC.

In addition, from the second FSMC, we obtained its distributor's invoices for purchases in 2 months of calendar year 2000 on behalf of an SFA with whom the second FSMC had a cost-plus-a-fixed-fee contract. We used the invoices to compare prices of 35 identical items purchased by both the second FSMC and the cited FSMC.

We also obtained information from one of the FSMC's vendors, a large food manufacturer, to verify that it had paid volume allowances to the FSMC.

In addition, we contacted State agencies in 22 States to obtain copies of the contracts, and the related RFPs/IFBs,[20] between the FSMC and/or its school food service sector and its 298 contracted SFAs identified in the documents we received from the company. See exhibit B for a list of the States.

- We also requested information concerning their State laws, policies, procedures, and memorandums issued to an SFA when contracting with FSMCs, and the State agencies' monitoring efforts to ensure an SFA met program requirements and the FSMC complied with contract terms.

- We also requested information about any State agency reviews of SFAs contracting with FSMCs, including the cited FSMC. We reviewed all of the contracts, RFPs/IFBs, and other information received from the State agencies.

Exhibit E illustrates the State agency policies and procedures they provided applicable to our audit period and any changes made to them.

We reviewed the Federal requirements for the NSLP/SBP for SFAs contracting with FSMCs to identify the FNS policies and operating procedures established for the contracts. We also conducted our review through interviews with officials of the FSMC and its school food service sector, FNS National office officials, State agency officials, and some SFA officials.

Also, we obtained billings of the FSMC for costs and fees from an SFA for January 2001 through June 30, 2001, to determine if costs and revenues projected by the FSMC for the school year ended June 30, 2001, were verified by actual data.

We determined from our review of the information provided by the FSMC that it received $3.1 million (rounded) in cash discounts and $3 million (rounded) in volume allowances, for a total of over $6 million in cash discounts and volume allowances based solely on purchases for SFAs in 22 States during the period July 1, 1998, through December 31, 2001. Company officials stated that none of the $6 million in cash discounts and volume allowances on the purchases for SFAs was passed through to those SFAs.

However, the scope of our review was limited by the fact that we could not determine from the material given to us by the FSMC on volume

[20] We asked only for contracts and RFPs/IFBs for SFAs that had contracted with the FSMC on a cost-plus-a-fixed-fee basis.

allowances what portion of the $3 million was attributable to purchases for each individual SFA. Company officials stated that their computer system could not identify the purchasing programs the company entered into in its FYs ending August 30, 1999, and 2000. In a June 2002 letter to us, the FSMC officials stated that, because they were not able to reproduce the exact national volume allowances for FY 1999 and 2000 due to system limitations, they estimated the national volume allowances for such FYs based upon companywide national volume allowances earned through their top volume manufacturers in those relevant years. In subsequent conversations, they stated that they were able to use current year purchase programs to determine the FY 2001 and FY 2002 first quarter national volume allowance information due to proximity of the years. Company officials stated that they could not go back to obtain information on the purchasing programs for FYs 1999 and 2000 because the programs were purged from the computer system when the purchasing programs for the new FY were entered. They said that the company kept no history files.

In addition, the FSMC's information on the other rebates included in the $3 million amount was only presented on a yearly total basis and was not broken down by SFA/cost center. As a result, the FSMC only broke down the FY 2001 and FY 2002 first quarter national volume allowances, which were $646,999 of the $3 million total in volume allowances received by the company and not passed through to SFAs. See exhibit C for a breakdown of how the company reported the $3 million in volume allowances.

The audit was performed from October 2002 through June 2005. The audit work was conducted in accordance with Government Auditing Standards.

Exhibit A – Summary of Monetary Results

Finding No.	Description	Amount	Category
1	FSMC Kept Discounts and Rebates	$6,126,830	Funds To Be Put To Better Use - Reviews of Contract/ Grant Agreements

Exhibit B – States We Contacted

STATE AGENCY	ALL INCENTIVES TO SFA PER CONTRACT 1/	CONTRACT DID NOT REQUIRE ALL INCENTIVES TO SFA 2/	CONTRACT NOT RECEIVED 3/, 4/, 5/
Arizona	2	5	0
California	0	1	0
Connecticut	1	5	5
Florida	0	1	0
Idaho	0	2	0
Kansas	0	1	0
Massachusetts	0	1	0
Michigan	64	0	34
Minnesota	1	1	1
Missouri	2	12	0
New Hampshire	0	1	0
New Jersey	0	46	2
New York	0	4	0
Ohio	0	11	4
Oregon	0	7	0
Pennsylvania	26	0	3
Rhode Island	0	3	0
South Carolina	7	0	0
Texas 6/	0	0	0
Vermont	0	3	0
Washington	3	29	0
Wisconsin	0	9	1
Totals	**106**	**142**	**50**

1/ SFAs signed contracts providing that all purchase incentives received by the FSMC were to be credited to the SFA. Where an SFA had more than one contract within the audit period, we used the latest contract. We did not receive the older contracts within the audit period for all 248 (298 less 50 in last column) SFAs.

2/ SFAs signed contracts that did not provide that all purchase incentives received by the FSMC would be credited to the SFA. Seven SFAs signed contracts providing that the FSMC would not invoice for food or would purchase food and supplies from vendors selected by the SFA but allowed the FSMC to do the purchasing and select the vendors. Where an SFA had more than one contract within the audit period, we used the latest contract.

3/ SFA contract either not provided or the contract provided was active after the audit period.

4/ SFA contract not provided for one SFA in New Jersey, four SFAs in Ohio, and one SFA in Pennsylvania.

5/ Contracts active after the audit period for four SFAs in Connecticut, one SFA in New Jersey, and one SFA in Wisconsin did not require all incentives to go to the SFA. Contracts active after the audit period for one SFA in Connecticut, 34 SFAs in Michigan, one SFA in Minnesota, and two SFAs in Pennsylvania required all incentives to go to SFA.

6/ When contacted, Texas State agency officials stated that all eight SFAs had fixed-price contracts; therefore, we did not request the contracts.

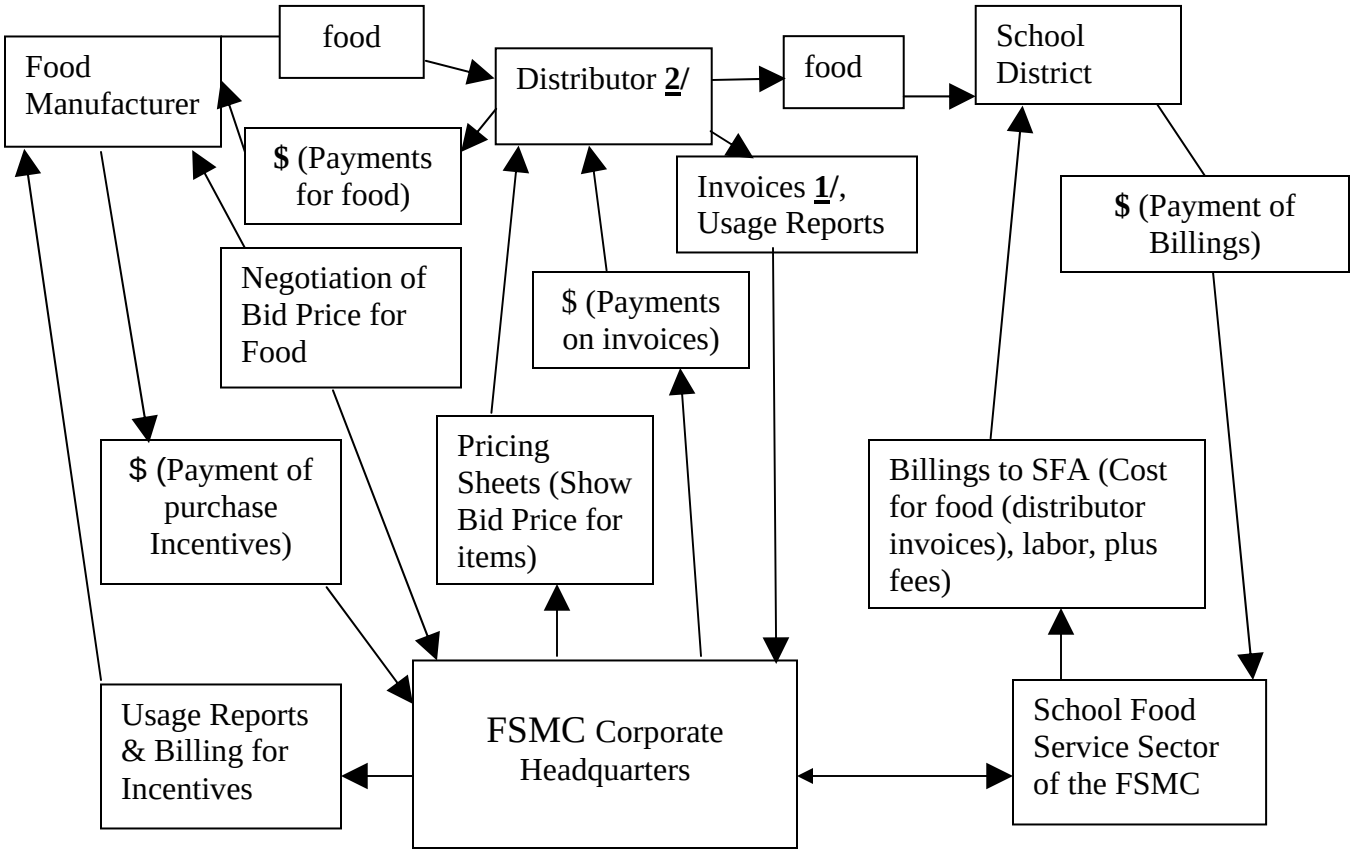
Exhibit C – *Purchasing Incentives Data Provided by an FSMC*

	FY 2002, 1st Quarter	**FY 2001**	**FY 2000**	**FY 1999**	**Total**
National Volume Allowances **1/**	$204,587	$ 442,412	$ 185,000	$ 70,000	$ 901,999
Local Rebates	$136,000	$ 275,000	$ 138,000	$ 130,000	$ 679,000
National Distributor Allowances Allocation	$103,000	$ 438,000	$ 485,000	$ 376,000	$1,402,000
Subtotal (Total Volume Allowances Received by FSMC)	$443,587	$1,155,412	$ 808,000	$ 576,000	$2,982,999
Cash Discounts Received by FSMC **1/**	$400,462	$1,243,659	$1,039,670	$ 460,040	$3,143,831
Total Incentives	$844,049	$2,399,071	$1,847,670	$1,036,040	$6,126,830

Note: FYs run from September 1 through August 30.

1/ The FSMC included some entities, which were not SFAs with cost-plus-a-fixed-fee contracts in its information on the purchasing incentives it received for NSLP/SBP related purchases. We have adjusted this information for the related cash discount information for FYs 1999 through FY 2002, 1st Quarter, and the related National Volume Allowance information for FYs 2001 and FY 2002, 1st Quarter.

FLOW OF MONEY AND FOOD[21]



1/ Invoices from distributor to the FSMC corporate headquarters include the bid price plus freight plus the distributor's markup. Usage reports from the distributor to the FSMC corporate headquarters would detail the volume of each product purchased (e.g. 200 cases of shoestring french fries). The FSMC corporate headquarters would forward usage reports along with a bill for incentives to the food manufacturer.

2/ We recognized that in some instances the distributor received a billback from the manufacturer. The distributor told us that they kept the billbacks and did not forward them on to the FSMC. Therefore, we ignored the billbacks for the purpose of our analysis.

[21] Food in this illustration means food, beverages, and supplies used in school food services.

FSMC Corporate Headquarters	Food Manufacturer	Distributor	FSMC School Food Service Sector	School Food Authority (SFA)
Negotiates bid price and purchase incentives with food manufacturer. Receives invoices and usage reports from distributor. Consolidates and pays distributor invoices for purchases, less any prompt payment discount, for all its (FSMC) sectors. Sends usage reports and billing for purchase incentives to food manufacturer. Receives payment for purchase incentives from food manufacturer for the period.	Negotiates bid price and purchase incentives with FSMC corporate headquarters. Ships food, and invoices to distributor. Upon receipt of usage reports and billing from FSMC corporate headquarters, sends payment for purchase incentives to FSMC corporate headquarters.	Receives pricing sheets, showing the bid price agreed upon with food manufacturer, from FSMC corporate headquarters. Upon receipt of food and invoices from food manufacturer, pays food manufacturer. Sends food to SFA(s). Sends invoices for bid price of food, and usage reports to FSMC corporate headquarters. Receives single payment from FSMC corporate headquarters for purchases by all FSMC sectors for the period.	Contracts with SFAs for operation of their school food services. Communicates with FSMC corporate headquarters. Sends monthly billings to SFAs for cost reimbursement and fees. Receives SFAs' payments on billings.	Contracts with FSMC school food service sector for operation of school food service. On-site school food service manager (usually employee of FSMC school food service sector) receives food from distributor. Receives billings for cost reimbursement plus fees from FSMC school food service sector. Pays billings from FSMC school food service sector.

Per the distributor's contract with the FSMC, the corporation pays for all of its sectors, including its school food service sector, in one lump sum check to the distributor.

The FSMC corporate headquarters negotiated contract terms, including the bid prices for food items, with food manufacturers. The contracts designated which distributors were used by the FSMC in particular areas. The FSMC corporate headquarters then sent bid pricing sheets to the distributor to use for invoicing food sent by the distributor to the FSMC's contracted SFAs. The bid pricing sheets showed only the bid price negotiated between the FSMC and the manufacturer, not the purchase incentives agreed upon between the manufacturer and the FSMC.

Upon receiving a purchase order, the food manufacturer sent the food to the distributor designated by the FSMC for the area covered by the purchase order. The distributor would distribute the food to the FSMC's SFAs, and send the invoices and usage reports to the FSMC corporate headquarters. The FSMC corporate headquarters in turn sent payment on the invoices, less any prompt payment discounts, to the distributor, and usage reports and a billing for the incentives to the food manufacturer. The food manufacturer then sent payment of the purchase incentives to the FSMC corporate headquarters. Meanwhile, the FSMC school food service sector sent monthly billings consisting of the cost of food, beverages, and/or supplies per the distributor invoices, labor, and administrative and/or management fees, to the SFA. The SFA then sent payments for the billings to the FSMC school food service sector.

STATE	POLICIES AND PROCEDURES DURING PERIOD JULY 1998 – DECEMBER 2001	POLICIES AND PROCEDURES AFTER DECEMBER 2001
AZ	The suggested pro forma contract did not mention purchase incentives.	The State agency encourages (but does not require) that contracts specify that all purchase incentives go to the SFA.
CT	The suggested pro forma RFP did not mention purchase incentives.	The State agency reviews SFA contracts but does not review if purchase incentives are covered.
FL	The sole SFA signed its contract before participating in the NSLP.	The State agency has issued a new required pro forma contract that provides that all purchase incentives go to the SFA.
ID	The State agency used the checklist in the FNS 1995 guidance for SFAs.	The State agency created an addendum for new contracts that specifies all purchase incentives must go to SFA.
KS	At the time that the only SFA's contract was awarded for the school year ended June 30, 2002, the State agency was not aware that language regarding purchase incentives needed to be in the contract.	The pro forma RFP required by the State agency provides that costs paid by the SFA shall be net of all incentives, but the required pro forma contract does not mention incentives. This State agency said that they have since been informed that OMB advises that SFA contracts with FSMCs are exempt from OMB Circular A-87 requirements.
MA	The State agency used the FNS 1995 guidance.	In the last 2 years, the State agency has sent recommended language for treatment of incentives to its SFAs. However, the SFAs are not required to use it.
MI	The State agency required its pro forma RFP/IFB to become the binding contract. The required RFP/IFB requires the FSMC to credit the SFA's food service account monthly for all discounts, rebates, and allowances received by the FSMC from the purchase of goods and services on behalf of the SFA. The SFA is responsible to ensure the FSMC is complying with the contract.	The State agency required RFP/IFB becomes the binding contract. The required RFP/IFB requires the FSMC to credit the SFA's food service account monthly for all discounts, rebates, and allowances received by the FSMC from the purchase of goods and services made on behalf of the SFA. The SFA is responsible to ensure the FSMC is complying with the contract. A requirement for the SFA to do quarterly internal reviews was effective for the 2002-2003 school year.

STATE	POLICIES AND PROCEDURES DURING PERIOD JULY 1998 – DECEMBER 2001	POLICIES AND PROCEDURES AFTER DECEMBER 2001
MN	The State agency used the FNS 1995 guidance.	In their letter of July 11, 2003, the State agency stated that during the last 2 years, it had developed an addendum, which must be signed by both the SFA and the FSMC, and be on file at the State Agency in order for the SFA to participate in the NSLP. The addendum, dated February 19, 2003, provides that the FSMC shall charge the SFA only for actual costs net of all purchase incentives.
MO	The State Agency used the checklist from the FNS 1995 guidance.	A State agency official wrote that their initial understanding was that the FSMC could charge costs only to the extent that they are allowable costs, net of all purchase incentives. The State agency was in the process of requiring SFAs to adopt an addendum to the contract that contained this language when they were contacted by some FSMCs. The FSMCs stated that their legal counsel had been in contact with USDA concerning this provision and the FSMCs maintained that the language did not apply to FSMC contracts with SFAs. The State agency then contacted the FNS Regional office, which stated that USDA did not have the authority to require this provision in the contracts. The FNS Regional office told the State agency that OMB had determined that its circular requirements for net costs (i.e., allowable costs must be net of all purchase incentives) do not apply to costs charged under the SFA contracts with FSMCs. The State agency official said that due to this information, the State agency does not review the contracts for treatment of incentive language and considers the responsibility for ensuring free and open competition on the contracts to be that of the SFAs.

STATE	POLICIES AND PROCEDURES DURING PERIOD JULY 1998 – DECEMBER 2001	POLICIES AND PROCEDURES AFTER DECEMBER 2001
NH	The State agency used the FNS 1995 guidance.	A State agency official stated that the contracts they are making now do address the purchase incentive issue, and that this information has been addressed in the contracts within the last several years.
NJ	FSMCs are required to register and send a "core contract" to the State agency and to note any changes to this contract for individual SFA contracts.	A State agency official said that FSMCs are expected to take advantage of local trade discounts and pass cost reductions on to SFAs.
OH	The State agency used the FNS 1995 guidance.	In a November 2002 memo to SFAs, the State agency stated that contracts that allow purchase incentives to go to the FSMC are prohibited, and that any current contracts with those provisions must be changed as of the next renewal or procurement action to read that all incentives go to the SFA.
OR	Oregon Administrative Rule, dated 1999, states that all rebates and discounts received by the FSMC from a third party must be refunded to the SFA. The State agency stated in their letter to us that it required SFAs to use its pro forma RFP and contract that provide that all purchase incentives are to go to the SFA. However, all but one of the contracts awarded during the audit period did not mention any treatment of purchase incentives. One contract excluded purchase incentives from corporate purchasing programs from being included in the requirements for incentives to be refunded to SFA.	SFA contracts awarded after the school year ended in 2002 require only that operating expenses shall be net of any incentives obtained from third parties for food, beverages, merchandise, and supplies procured **solely** (emphasis added) for the SFA's nonprofit food service. Also, one SFA's contracts for 2 school years ended in 2003 and 2004 specifically excluded cash discounts relating to payment terms and volume rebates paid to the FSMC as a result of FSMC corporate purchasing arrangements and not exclusively relating to products or items used on behalf of the district.

STATE	POLICIES AND PROCEDURES DURING PERIOD JULY 1998 – DECEMBER 2001	POLICIES AND PROCEDURES AFTER DECEMBER 2001
RI	The State agency policy is that the SFAs follow Federal regulations.	After a Management Evaluation by FNS disclosed some major concerns with the FSMC contract process, the State agency updated its contract review process in June 2002. The State agency decided to let existing contracts run their course and require its pro forma RFP and contract, issued in February 2003, for new contract awards. The pro forma RFP and contract now require the FSMC to pass along to the SFA all of the purchase incentives received on the FSMC's purchases on behalf of the SFA's food service. The contract requires the FSMC to document all incentives received on their monthly invoices to the SFA. Note: a third FSMC stated that it would show all the incentives received but will also bill the SFAs for the amount of the said incentive.
VT	The State agency provided pro forma RFP and pro forma contract did not mention purchase incentives.	A State agency official said that they began reviewing the contracts for treatment of purchase incentives after Office of Inspector General (OIG) requested contract information in our June 18, 2003, letter. The official said that they had not reviewed the contracts for the treatment of purchase incentives before our letter.
WA	The State agency provided pro forma RFP and contract checklist did not mention purchase incentives.	A State agency official stated that 7 CFR 210.19(a)(6) does not allow the State agency to approve contracts; it only allows them to review contracts. The official also stated that 7 CFR 210.16 does not grant the State agency the authority to require that contracts specify purchase incentives be passed back to the SFAs.
WI	The State agency provided pro forma IFB, contract, and contract checklist did not mention purchase incentives.	The State agency obtained advice from their FNS Regional office that the State agency should wait on USDA to provide guidance concerning the treatment of incentives. The State agency reviews the SFAs' RFPs and contracts.

United States Department of Agriculture

Food and Nutrition Service

3101 Park Center Drive

Alexandria, VA 22302-1500

OCT 29 2005

SUBJECT: National School Lunch Program – Cost-Reimbursable Contracts with a Food Service Management Company

TO: Robert W. Young
Assistant Inspector General
for Audit

We are responding to your August 17, 2005, memorandum transmitting the official draft of the above-referenced audit report from the Office of Inspector General. I appreciate the opportunity to comment on the draft report.

While we agree with auditors' conclusions in a number of areas within the report and will be working to implement corrective action for the problems noted, we disagree with OIG's statements on prompt payment and earned income discounts. The current draft refers to these payments as examples of volume purchase incentives that the Food Service Management Company (FSMC) is not entitled to receive either by contract stipulation between the School Food Authority (SFA) and the FSMC or by Federal policy. While OIG is correct in stating that the contract between the SFA-FSMC will control the disposition of such amounts, in the absence of specific contract terms, Agency policy only prohibits the retention of earned income or prompt payment discounts earned by the FSMC when the amounts are earned using funds advanced by the SFA. In addressing OIG's findings, we will direct State agencies to work with their SFAs to evaluate FSMC contract compliance pursuant to the terms of those contracts. As in any similar situation, when unallowable nonprofit school food service account expenditures are identified, one element of the accepted corrective action is the restoration of these amounts to the affected nonprofit school food service accounts. However, we cannot require that State agencies direct SFAs to restore funds to the nonprofit school food service account for expenditures that are otherwise allowable. I am disappointed that we were not able to achieve agreement on this point.

The present design of the chart found in Exhibit D (a flow-chart attempting to illustrate the corporate practices found in some FSMCs as well as other similarly structured businesses) does not effectively demonstrate the concepts/relationships that OIG wishes to present in this report. We believe that the present chart attempts to cover too much information to be readily comprehensible to the general reader; we believe that the essential information can be presented more simply.

Robert W. Young 2

Please review the general use of regulatory citations in the body of the report. In a number of places, the citations provided by OIG no longer match up with the subsequent discussion of requirements or controls. We believe that this may have happened as material was altered or deleted in the development of the report from its earliest draft to its current version. While not disruptive to the general reader, this may adversely impact staff at the State or SFA who will use the report to evaluate findings or develop corrective action or policy. My staff is available to provide more detailed illustrations of this problem.

Please feel free to contact my staff or I should you have any questions on our comments.

Roberto Salazar
Administrator

Glossary of Terms

Billback	-	The amount a distributor "bills back" to a manufacturer representing the difference between the price the distributor paid the food manufacturer for an item and the lower price negotiated between the FSMC and the food manufacturer. For example, the food manufacturer negotiates with the FSMC to allow the approved distributor to bill back to a price of $9 on the volume sold to the FSMC. On a direct sale to the distributor at the highest bracket delivered price of $12, the manufacturer earns $12 per case. On the volume sold to the FSMC, the distributor bills back $3 per case, so the manufacturer nets $9, as agreed. The price to the FSMC is the net $9, plus freight and the distributor's markup to the FSMC.
Cost-plus-a-fixed-fee contract	-	A contract that provides for the SFA to reimburse the FSMC for its costs plus a fixed amount per meal for administrative and/or management fees.
Fixed-price contract	-	A contract that provides for the SFA to pay the FSMC a contractual rate per meal for certain categories of meals (e.g., reimbursable lunches).
Discount	-	A reduction from the full or standard amount of a price or debt.
Rebate	-	A deduction from an amount charged or a return of part of a price paid.

Informational copies of this report have been distributed to:

Administrator, Food and Nutrition Service	
Director, Grants Management Division	(8)
Office of the Chief Financial Officer	
Director, Planning and Accountability Division	(1)
Government Accountability Office	(1)
Office of Management and Budget	(1)