

# **MUNICIPAL AUDITING REPORT CITY OF ROANOKE**



## **Audit of School Food Services October 4, 2019**

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Audit Plan Number: 19-103

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## AUDIT OBJECTIVES & SCOPE

1. To identify any impact on student participation, financial viability of the food services fund and utilization of local suppliers that might be associated with outsourcing the food services function.

*Conclusion: Student participation under Sodexo has remained comparable to participation levels prior to outsourcing as data on meals served shows relatively consistent purchase volume. Participation increased significantly during FY2016 when RCPS began participating in the Community Eligibility Provision (“CEP”) as free meals were available to all students at 19 of 26 sites. Strong participation in turn is allowing the food services fund to be strong financially as revenues from activities exceed operating costs. Our analysis of spending with local suppliers indicated utilization was substantially the same or greater after outsourcing.*

2. To determine if Sodexo billed the School Division in accordance with the terms and conditions of the contract.

*Conclusion: Costs billed in FY2018 were materially correct and consistent with the contract. We identified \$8,158 in credits mistakenly entered as charges; an adjustment was posted on the February 2019 invoice that corrected the identified error. Division management conducted regular site visits, but did not perform quarterly internal audits of food, labor, and other large expense items as specified in the contract with Sodexo. Management should strengthen its processes for monitoring contract compliance and allowable costs, including requiring more informative budgets and better information on the origin and nature of cost components from Sodexo.*

3. To determine if meal equivalents were accurately reported.

*Conclusion: Appropriate controls are in place to help ensure meal count data is accurately reported to the USDA for reimbursement claims, and serves as a valid basis for Sodexo’s administrative and management fees. Required annual accountability reviews should be completed more timely and no later than February 1.*

4. To determine if Sodexo has appropriate inventory procedures in place for both purchased and USDA donated foods.

*Conclusion: The existing inventory system and processes are reasonably sound and help ensure food and supplies are accounted for and stored consistent with USDA requirements. The inventory process is not designed to identify losses from waste or misappropriation. Other processes may be needed to control for overproduction, spoilage, and shrinkage.*

Audit Scope:

We evaluated the design of processes for monitoring vendor performance and billings that were in place as of September 1, 2018. We tested the effectiveness of these processes based primarily on operations from July 1, 2017 through June 30, 2018. We visited a number of schools at the end of October 2018 in order to observe the inventory process that serves as the basis for billing the cost of food to the Division each month.

Our analysis of historical financial and participation trends covered July 1, 2014, through June 30, 2018. We utilized data from the Virginia Department of Education to compare RCPS with other localities in the area or with similar demographics:

- Roanoke County
- Montgomery County
- City of Lynchburg
- City of Richmond

**End of Audit Objectives and Scope**

## BACKGROUND

Roanoke City Public Schools (RCPS) Department of Food and Nutrition operates a variety of programs to meet their mission. These include:

- National School Lunch Program
- School Breakfast Program
- Summer Food Service Program for children
- Child and Adult Care Food Program
- Fresh Fruit & Vegetable Program

The National School Lunch Program (NSLP) and School Breakfast Program (SBP) are the largest programs administered by RCPS. These programs provide meals to RCPS students throughout the division during regular school days. In FY2018 (July 1, 2017 – June 30, 2018) RCPS served 1,721,344 lunches and 983,402 breakfast meals across 26 different schools in the district.

Each of the programs listed above are federally administered by the United States Department of Agriculture. At the state level the Virginia Department of Education Office of School Nutrition provides oversight and administration to all Commonwealth localities.

### Outsourced Food Services with Sodexo

In April 2016, the Division contracted with SodexoMAGIC (“Sodexo”) to manage its food services operations. Sodexo invoices the Division for all costs, including personnel, supplies, insurance and systems related expenses. The company also bills an administrative and management fee based on meal equivalents served. The contract requires that Sodexo generate a minimum financial return for the Division each year. The required minimum return specified for FY17, FY18, and FY19 was ~ \$484,000 per year. The Division may recover any shortfall from Sodexo, up to 100% of the administrative and management fees earned. A return is necessary to fund utilities, maintenance, and capital equipment costs.

The Division continues to employ two (2) positions to monitor contractor performance, complete required reporting, and satisfy other specified regulatory tasks. While planning the audit, we reviewed requirements stated in the contract, federal regulations pertaining to oversight of food services management companies (*7CFR 210.16*), and the role of the Director and Assistant Director of Food Services in monitoring contractor performance and compliance with contract terms.

Some of the primary monitoring requirements were incorporated into the various audit objectives. Other aspects were reviewed during planning but were not subject to audit. We noted the following during planning pertaining to the school food services advisory board:

Advisory Board:

Federal regulations require school divisions using food service management companies to establish an advisory board composed of parents, teachers and students to assist in menu planning. The contract with Sodexo provides for an advisory board and requires Sodexo to participate in the board's meetings.

RCPS formed a Food Services Committee that met for the first time in November 2016. While it includes a parent and teachers, it does not satisfy the requirement to include a student member. There is no committee charter outlining its purpose and goals or the expectation that it satisfy the federal requirements for an advisory board. Committee minutes indicate substantive discussions are taking place. It had met five (5) times from November 2016 through September 2018. The Committee expected a Student Advisory Council to be created for the 2018/19 school year.

Food Quality and Inspections:

One of the stated goals of outsourcing was to improve the quality of the food served. USDA regulations also contain complex requirements regarding the required meal components along with the nutritional components associated with food served in USDA programs. We discussed both topics with management at length while planning the audit.

The VDOE and Department of Agriculture performed compliance audits in 2017 that looked at meal patterns, safe handling and storage of foods, and other aspects of food services. Both reports were complimentary with minimal findings noted. The Health Department regularly inspected all school cafeterias and upon review, we noted no critical issues were cited.

Management felt that the variety and quality of foods had improved based on their school visits and work with the dietician. In 2017, Sodexo surveyed teachers and staff, principals and students about food selection, quality, cost, and service. Response rates were too low to be representative of the overall population and draw conclusions on quality of food options under Sodexo:

- Teachers/ Staff = 37
- Elementary Students = 21
- Secondary Students = 47
- Principals = 13

Community Eligibility Provision:

Roanoke participates in the USDA's Community Eligibility Provision (CEP) program authorized under the "Healthy, Hunger-Free Kids Act" in 2010. Schools qualify based on the proportion of students participating in benefit programs such as the Supplemental Nutrition Assistance Program ("SNAP"), Temporary Assistance for Needy Families ("TANF"), Foster Care, Head Start, and similar programs. Students attending CEP designated schools receive free breakfast and lunch regardless of their ability to pay.

Nineteen (19) of 26 schools in the Division were designated as CEP participants for FY16, 17 and 18. Beginning in August of 2018, all of the Divisions schools qualified for CEP designation, except for Crystal Spring and Grandin Court. Students attending these two elementary schools can still qualify for free or reduced priced lunches through the traditional eligibility application process. In 2017-18, 86.9% of RCPS students participated in the free lunch program. This represents an increase of 17% from the 2015-16 school year.

**End of Background**

### Objective 1: Participation, Financial Viability & Local Suppliers

We compared RCPS with other school divisions both before and after outsourcing operations to Sodexo. The following divisions (each of which maintains food service operations in-house) were selected to provide a diverse comparison with regional and urban school systems:

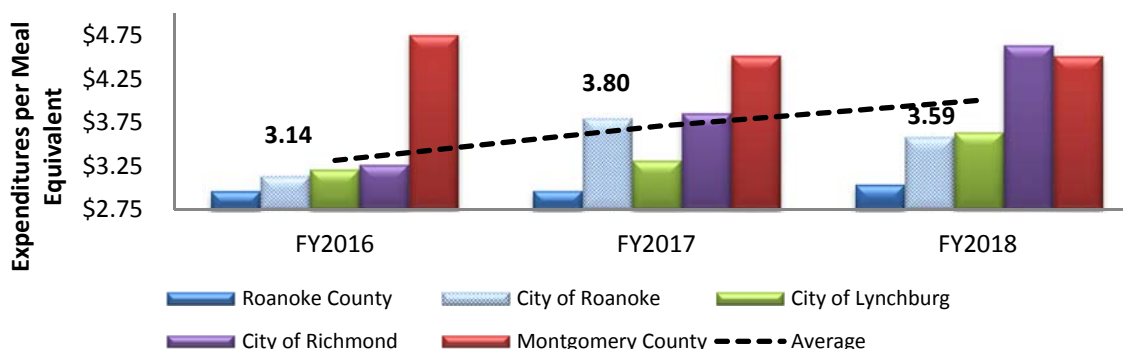
- Roanoke County Public Schools
- Montgomery County Public Schools
- City of Lynchburg Public Schools
- City of Richmond Public Schools

The Office of School Nutrition Programs within the Virginia Department of Education provided the meal count and financial data filed by the selected divisions for FY16, FY17, and FY18.

#### Expenditures per Meal Equivalent

Data shows RCPS has comparable costs on a meal equivalent basis. RCPS experienced a substantial increase in the cost per meal equivalent during the first full year managed by Sodexo. The per meal costs returned to a comparatively competitive level in FY18.

**Expenditures per Meal Equivalent Comparison**

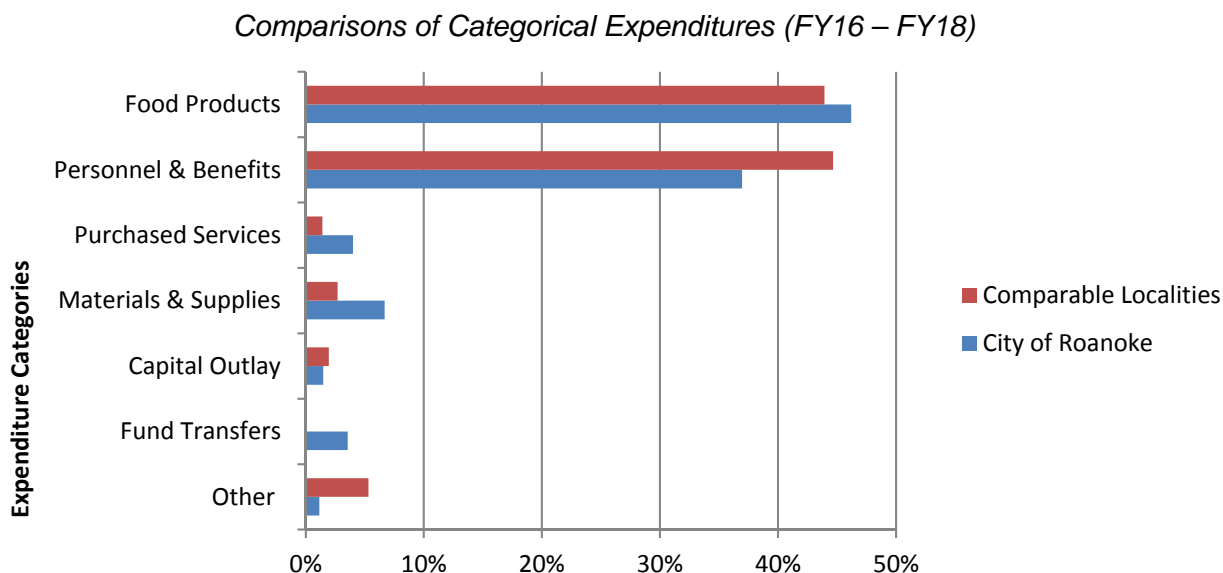


Meal equivalents is a standard benchmarking tool in the food service industry to assess costs in relation to volume. The contract between RCPS and Sodexo also incorporates meal equivalents to calculate management and administrative fees. Based upon the contract, which follows VDOE guidelines, the following formula determines meal equivalents:

Lunch	<ul style="list-style-type: none"> <li>• Determined by actual count</li> <li>• 1 lunch served = 1 meal equivalent</li> </ul>
Breakfast	<ul style="list-style-type: none"> <li>• Actual count divided by 2</li> <li>• 2 breakfasts served = 1 meal equivalent</li> </ul>
Afternoon snacks	<ul style="list-style-type: none"> <li>• Actual Count divided by 4</li> <li>• 4 afternoon snacks = 1 meal equivalent</li> </ul>
Suppers	<ul style="list-style-type: none"> <li>• Determined by actual count</li> <li>• 1 supper served = 1 meal equivalent</li> </ul>



Using Sodexo’s operating statements, we translated expenditure data into a common format that allowed us to compare categorical expenditures with other school divisions over the combined three fiscal years (FY16 thru FY18) to assess food service component costs over a long-term period:



RCPS used Elwood Staffing to provide much of its cafeteria staff prior to engaging Sodexo. Payments to Elwood were classified as “Purchased Services” and accounted for \$904,250 (~ 80%) of purchased services in FY16. As such, purchased services appear somewhat higher and personnel and benefit costs lower. Actual spending on personnel is more comparable to other localities.

The higher proportion of personnel costs for comparable localities also appeared to be driven by Montgomery County. They were an outlier, reporting ~ 34% food costs and ~ 54% personnel related costs. Other benchmark localities were more comparable with RCPS.

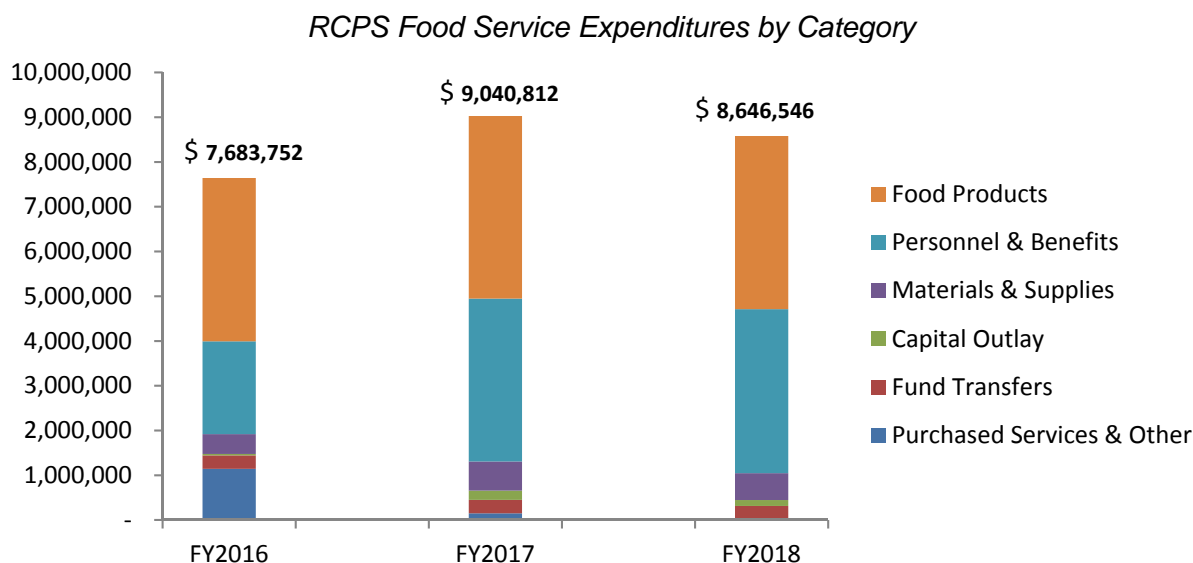
RCPS reported a notably higher proportion of materials and supplies costs, partly due to using compostable trays that cost ~ \$0.09 each versus \$0.03 for more commonly used disposable trays. Based on ~ 2,700,000 breakfast and lunch meals served in FY18, the incremental cost for compostable trays was ~ \$162,000.

**Higher supply costs, driven by use of compostable trays, incrementally cost \$162,000 annually**

The “Fund Transfers” and “Other” expenditures were similar in nature and could be considered one combined category. RCPS transferred \$300,000 annually to the general fund to reimburse utility and other facility costs associated directly with the cafeteria. These types of expenses were billed as internal service charges in other divisions and reported as “Other” expenditures.

RCPS Costs Before and After Sodexo

The transition to Sodexo began during the summer of 2016 (very end of FY2016). Sodexo began preparation for managing RCPS food services in April 2016 and was responsible for providing meals to students enrolled in RCPS+ that summer. We compared costs categorically in the year prior to transition (FY2016) and the subsequent two years:



The chart shows that food services expenditures increased by \$1,357,060 during Sodexo's first full school year. Based on the available data and management's feedback, we identified the following contributing factors:

**Costs rose by \$1.35M in transition to outsourcing with Sodexo – Management & Admin fees attributed \$587k**

**Contract fees are designed to cover administrative costs incurred by Sodexo – also provide profit to Sodexo**

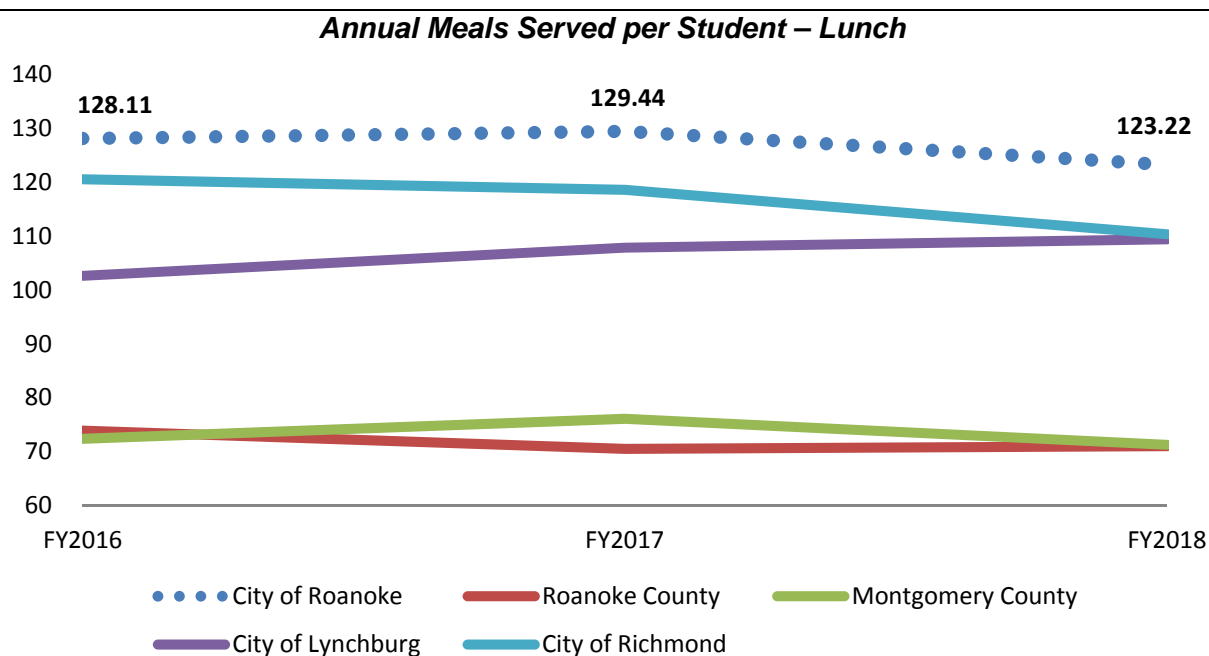
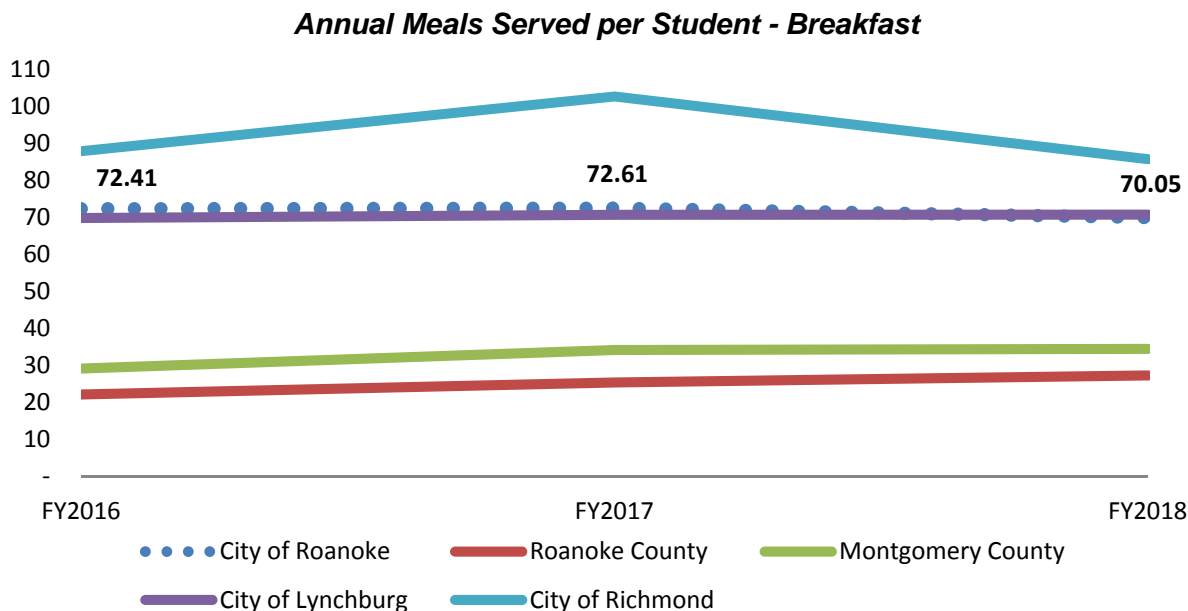
Description	Amount
Sodexo Admin & Management Fees (\$0.238 per meal equivalent)	587,000
Expansion of Fresh Fruits & Vegetables Program	91,050
Increased Meals & Inflation	70,000
Additional Capital Outlays for Needed Upgrades to Equipment	142,500
<b>Total:</b>	<b>890,550</b>

Additional factors in the increase costs may have been one-time setup costs incurred by Sodexo in their first full year along with improved product quality. Discussions with management indicated they were aware of Sodexo putting higher quality items on the menu. We were unable to quantify the impact of these factors.

FY18 costs declined ~ \$394,000 overall, largely due to reductions in costs for food, materials & supplies, as well as capital outlays. Personnel and benefit costs were relatively flat with reduced costs of benefits offsetting a 2% pay raise.

Annual Meals Served per Student – Breakfast and Lunch

Using “meals served” and “average daily membership” data from the VDOE, we analyzed the relative level of participation in the school breakfast and lunch programs among our benchmark school divisions.



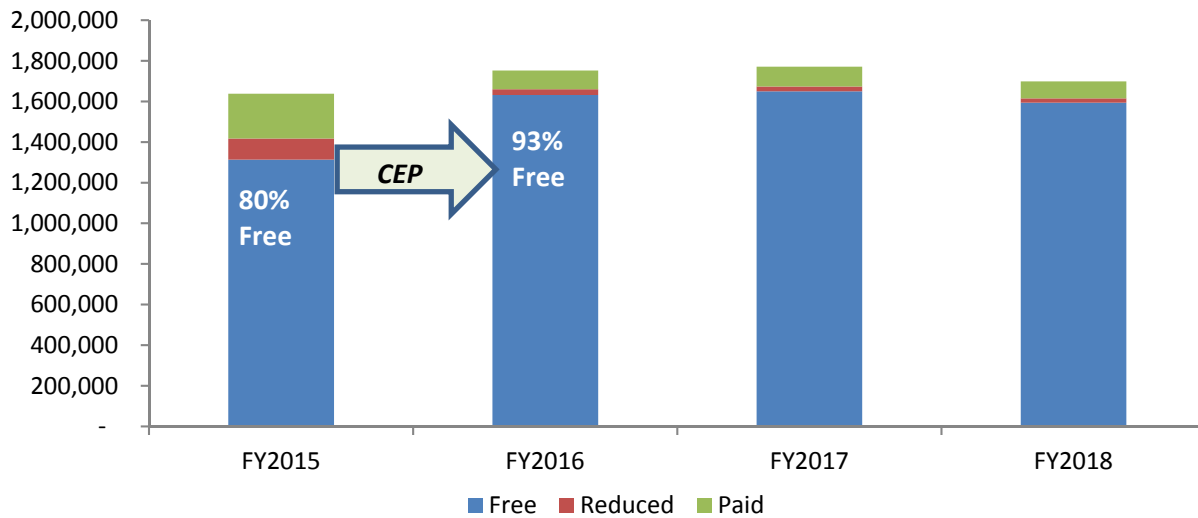
Meal participation is affected by a variety of factors such as food quality and variety, time allowed to eat, length of lines, and cost. CEP also made meals free for 100% of students at designated schools. Data shows cost appears to significantly impact participation as the school divisions with higher participation generally were those participating in CEP. The following table

shows the proportion of students at our benchmark divisions that were in CEP designated schools as reported by the VDOE in FY17:

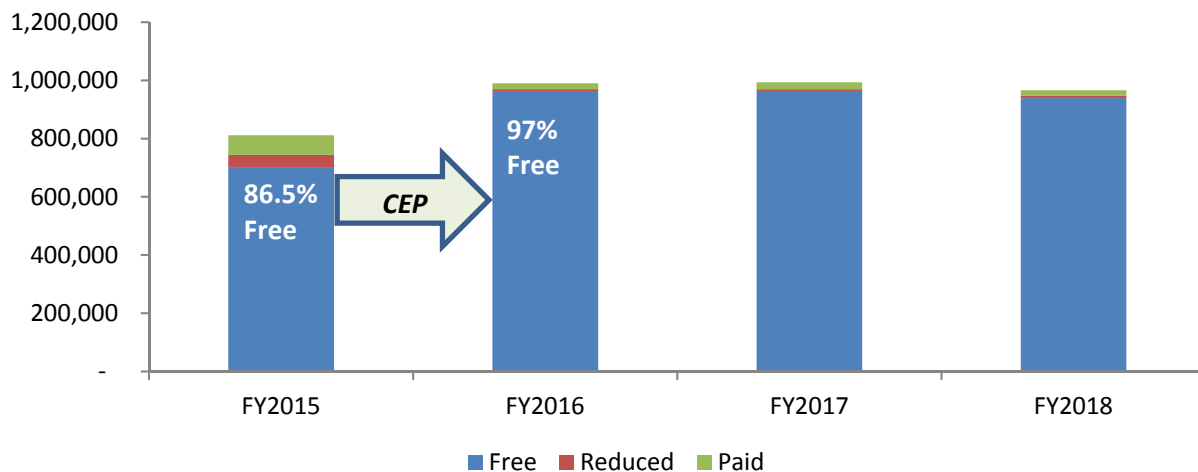
School Division	CEP %
Roanoke County	0.00%
Montgomery County	0.00%
City of Lynchburg	40.30%
City of Roanoke	69.80%
City of Richmond	100.00%

Roanoke City had 19 of 26 schools participating in the CEP program beginning in FY16. Meal count data shows CEP participation boosted the number of meals served in by RCPS in FY16, increasing breakfast and lunches served annually by 18% and 7%, respectively, with the boost sustained through FY18:

**Lunch Meals Served Trend**



**Breakfast Meals Served Trend**

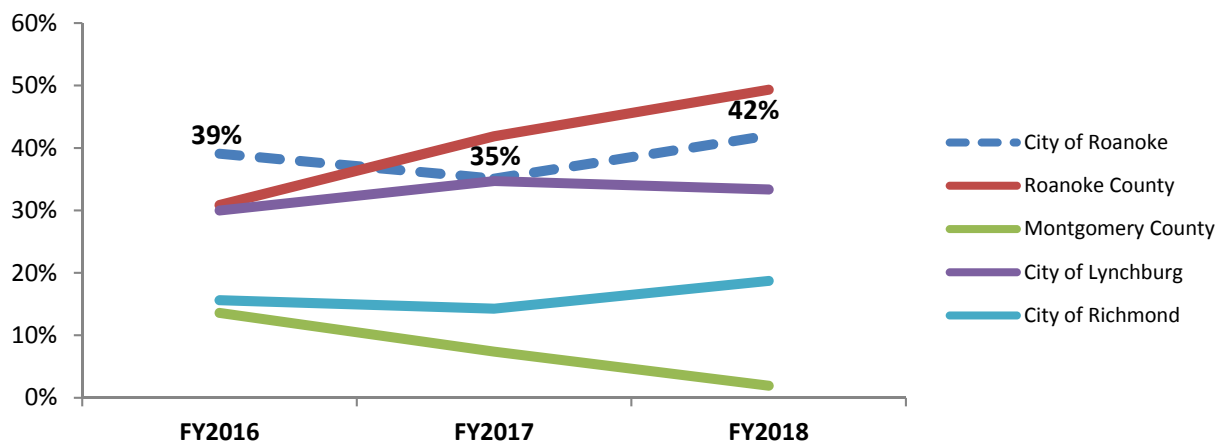


Percentage of Fund Balance to Annual Expenditures

The percentage of fund balance to annual expenditures measures the financial stability of operations. School food service funds are designated as self-sustaining, meaning they are supported by revenues from operations (primarily federal reimbursements associated with meals served) instead of being reliant upon local tax revenue and general subsidies for financial support. A healthy fund balance is necessary to finance capital equipment replacements and absorb unanticipated deficits when revenues and expenses don't perform as forecasted.

Based on the annual financial reports (SNP020) school divisions file with the VDOE, we compared fund balance trends in relation to annual expenditures.

**Percentage of Food Services Fund Balance to Annual Expenditures**



Our analysis shows that fund balance was temporarily affected by the FY17 increase in expenditures, but quickly recovered to a comparatively healthy level in FY18. At 42% of annual expenditures, RCPS had sufficient fund balance to cover five (5) months of operations.

Requirements in 7CFR 210.14(a) actually stipulate that a *school food authority shall limit its net cash resources to an amount that does not exceed 3 months average expenditures for its nonprofit school food service*. In Board action on February 26, 2019, management presented \$550,700 of planned capital spending to utilize the surplus funds and bring fund balance within the regulatory requirements, as well as address capital needs in the various schools.

Local Vendors

One concern associated with outsourcing food services was about the impact on local vendors who historically supplied dairy, fruits, and other food and supplies. To address this concern, the Board included a stipulation in the contract requiring the use of local vendors to source food and supplies when possible. “Local” was defined as being within 60 miles of the City of Roanoke.

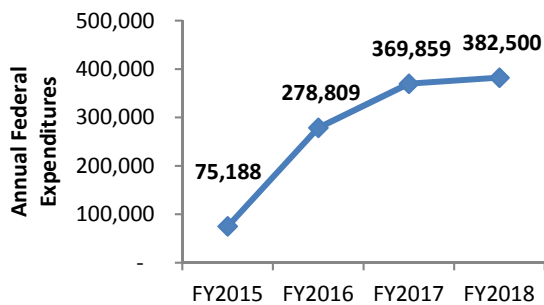
Expenditure data shows Sodexo maintained relationships with local vendors as required contractually. The following table shows expenditures for food and supplies prior to outsourcing (FY15) compared to Sodexo’s expenditures in FY18:

Vendor	Product	FY15		FY18	
US Food Roanoke√	Food	2,290,435	59%	2,763,274	59%
United Dairy√	Milk and Juice	596,104	15%	550,629	12%
Roanoke Fruit & Produce√	Produce	283,873	7%	440,574	9%
General Sales of Virginia√	Paper and Plastic	240,900	6%	353,800	7%
Flowers Baking Co Lynchburg√	Baked Goods	102,305	3%	122,523	3%
Crook Brothers Produce①	Produce	-	0%	307,599	7%
Other		396,796	10%	148,172	3%
<b>Totals:</b>		<b>3,910,415</b>	<b>100%</b>	<b>4,686,575</b>	<b>100%</b>

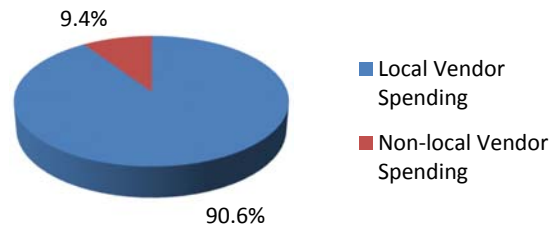
√ Meets criteria for “local vendor” designation

① Crook Brothers is a West Virginia based vendor who provides much of the produce for the federal *Fresh Fruit and Vegetable Program*. RCPS has been able to expand this program from 3 to 11 schools from FY15 to FY18 with additional funding (as shown below). This has resulted in additional expenditures with Roanoke Fruit & Produce as well.

**Fresh Fruit & Vegetable Program Expenditures**



**Local Vendors Share of the Pie**



**End of Objective 1**

## **Objective 2: Sodexo Invoicing**

Did Sodexo bill the School Division in accordance with the terms and conditions of the contract?

### **Contract Oversight**

Federal Regulations require RCPS to perform monitoring activities over Sodexo as a food service management company. Federal regulations stipulate that when a food service management company is utilized, the local school division retains responsibility for ensuring food service operations are conducted in conformance with agreements for the program. The local school division also retains control over the quality, extent, and general nature of food services.

The contract with Sodexo stipulates that RCPS “shall conduct an internal audit of food, labor, and other large expense items quarterly as well as perform random audits on smaller expense items.” We found that the Director and Assistant Director of Food Services had reviewed and approved monthly invoices and supporting operating statements from Sodexo. However, they had not developed a program for performing quarterly audits of expenses or documented any formal reviews.

The contract also specifies that Sodexo must provide a budget for the upcoming school year no later than December 15. The budget must address prices, labor and food costs, and demonstrate the ability for the fund to be self-supporting. The School Board retains ultimate control over the adopted meal prices and costs for food services.

We found that management did not have a copy of the Sodexo budget for the current year, which should have been provided prior to December 15, 2017. We reviewed the budget provided in 2016 and found it was a one-page document. The names used for several budget items were not self-explanatory and were not elsewhere defined. The budget did not include prior year data for comparison purposes. There were no notes about assumptions on which the budget was based, significant changes from prior years, or other insight to enable proper review and understanding of the budget. It was largely on this basis that management had instead relied on alternative information, similar to that used prior to outsourcing, for budget planning.

### **Overview of Food Services Billings**

Sodexo provides a monthly invoice to the Director of Food Services along with an operating statement breaking out revenues, expenses and meal counts. Expenses are broken down into four components:

**Product Costs**

- The cost of food consumed in operations during the month as tracked through Sodexo’s inventory system. These purchases should be net of any vendor discounts and rebates negotiated by Sodexo.

**Labor**

- Cost of salaries, benefits, payroll taxes, and payroll processing costs for all Sodexo staff working at RCPS.

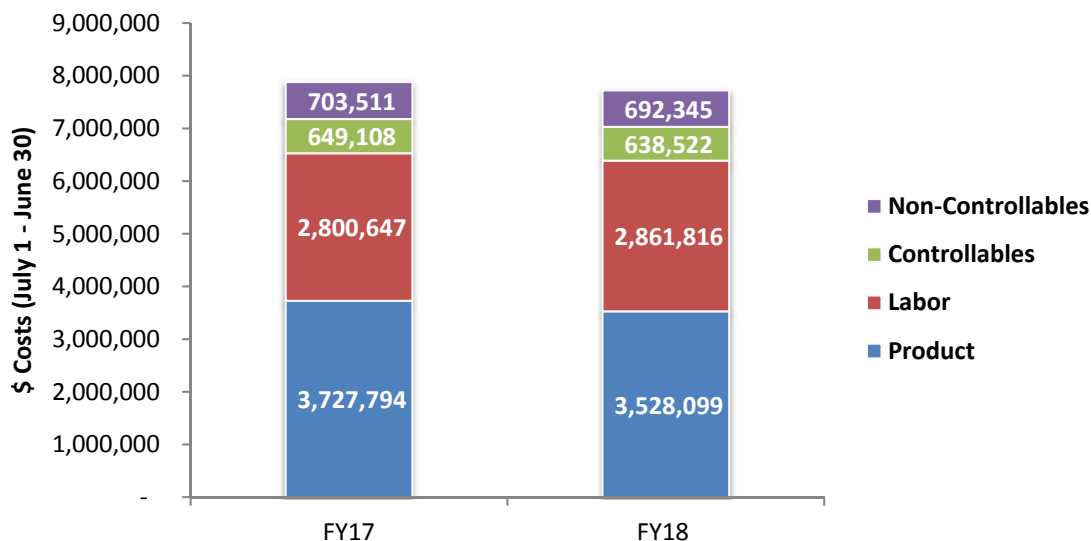
**Controllables**

- Materials and supplies, administrative costs such as background checks and training, and asset depreciation directly associated with RCPS operations.

**Non-controllables**

- Corporate costs for insurance, amortization, information systems, etc., that are allocated by formula to clients. Also reported as part of this component are “Administrative and Management” fees based on meal equivalents served.

Based on Sodexo’s June 2018 operating statement, we compared costs on a line-by-line basis, as follows:



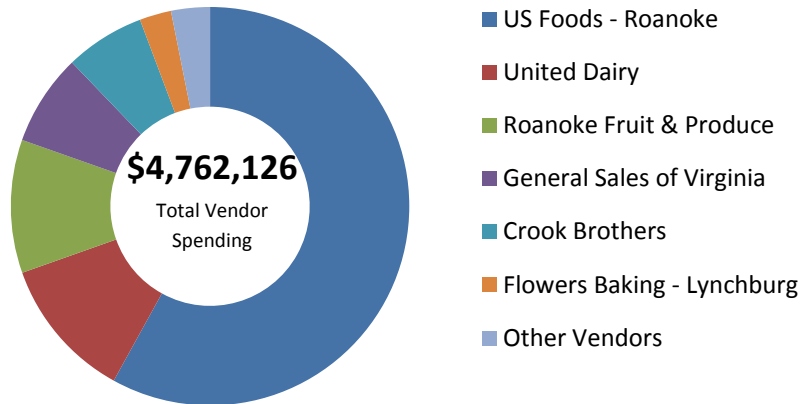
Overall costs declined approximately 2% in FY18 due in part to a comparable 2% decline in meals served. Labor increased approximately 2%, which was consistent with raises given to food services employees.

**Vendor Confirmations of Annual Expenditures**

Based on Sodexo’s accounts payable register for FY18, six (6) vendors accounted for 96.9% of the overall spend on food and supplies:



### Vendor Spending FY2018



Our office sent confirmation requests to these six vendors to verify the costs reported by Sodexo. We compared their reported costs to Sodexo’s financial records:

Vendor	Purchases Confirmed	Sodexo's Records	Confirmation Variance	Confirmation % Variance
United Dairy	550,049.73	550,629.89	580.16	0.11%
US Foods - Roanoke	2,754,509.51	2,763,274.94	8,765.43	0.32%
Roanoke Fruit & Produce Co.	514,328.69	514,438.80	110.11	0.02%
General Sales of Virginia, Inc.	350,782.90	353,800.16	3,017.26	0.85%
Flowers Baking Co. of Lynchburg	122,640.73	122,523.81	(116.92)	-0.10%
Crook Brothers Produce	301,251.23	307,599.64	6,348.41	2.06%
<b>Total</b>	<b>4,593,562.79</b>	<b>4,612,267.24</b>	<b>18,704.45</b>	<b>0.41%</b>

We viewed the overall variance as being immaterial. However, we undertook additional reviews of US Foods and Crook Brothers Produce based on them having the more significant dollar variances.

- US Foods – The confirmation did not include delivery and minimum order charges billed by US Foods to Sodexo.
- Crook Brothers – We identified \$5,733 in Sodexo’s purchase detail that was supported by physical invoices but had not been captured in Crook Brother’s confirmation.

This reduced the overall variance to less than 0.1% of expenditures. These confirmations provided assurance that costs captured in Sodexo’s accounts payable register for FY18 were accurate.

## Sample Testing

We audited the September 2017 and April 2018 invoices and accompanying Sodexo operating statements as a basis for verifying amounts billed were appropriate and supported. These two months covered approximately 19.3% of the overall costs billed for FY18:

	Sep-17	Apr-18	Total Tested	Annual FY18 Expenses	Testing %
<b>Product Costs</b>	461,480	253,628	715,108	3,528,099	<b>20.3%</b>
<b>Labor</b>	267,662	246,700	514,362	2,861,816	<b>18.0%</b>
<b>Controllables</b>	63,250	56,964	120,214	638,522	<b>18.8%</b>
<b>Non-Controllables</b>	75,216	61,738	136,954	692,345	<b>19.8%</b>
<b>Total Expenses</b>	<b>867,608</b>	<b>619,030</b>	<b>1,486,638</b>	<b>7,720,782</b>	<b>19.3%</b>

We began by reconciling Sodexo's operating statements with the associated invoices, noting the following:

- Overall amounts billed on the invoices matched the Operating Statements.
- Vendor discounts on the Operating Statement agreed with those shown on the monthly invoices.
- Sodexo explicitly certified no unallowable costs were charged, as required in *Contract Section 2.17(J)(4)*.

The Director of Food Services had signed both invoices signifying her review and approval.

### Product Costs:

We traced Sodexo's cost as recorded in its accounts payable register, through its monthly client revenue and expense detail report, to the monthly operating statements and invoices.

Cost Component	September 2017	April 2018
Unit Transmittals & Electronic Invoices	501,573	324,462
P-Card Purchases & Expense Reports	3	226
Journal Entries	5,719	2,849
Other	5,218	-
<b>Gross Product Costs</b>	<b>512,513</b>	<b>327,537</b>
Monthly Inventory Change	-	(14,748)
Transfers – Fresh Fruit & Vegetable Program	(28,454)	(36,205)
Vendor Discounts	(22,578)	(22,956)
<b>Net Product Costs</b>	<b>461,481</b>	<b>253,628</b>

In comparing the unit transmittals and electronic invoices posted in the A/P Register (verified as accurate through our vendor confirmations) to those in the client revenue and expense detail report, we identified only immaterial differences in total costs:

<u>September 2017</u>	<u>Expense Detail</u>	<u>A/P Register</u>	<u>Variance</u>
Electronic Invoices	386,830.37	386,830.37	-
Unit Transmittals	176,618.18	176,008.52	609.66

<u>April 2018</u>	<u>Expense Detail</u>	<u>A/P Register</u>	<u>Variance</u>
Electronic Invoices	262,200.17	262,200.17	-
Unit Transmittals	107,480.41	107,480.41	-

Amounts on the client revenue and expense detail were consistent with the operating statements and invoices received by RCPS. In combination with our confirmation procedures, we find that the costs billed for food and materials in the months tested were materially correct.

The remaining cost components were evaluated as follows:

- Journal Entries, P-Card Purchases and Expense Reports were immaterial and did not warrant further review.
- “Fresh Fruit & Vegetable Transfers” were determined to be appropriately billed in separate invoices. Monthly, Sodexo transfers costs related to Fresh Fruit and Vegetables from their general unit to another unit for billing. As RCPS utilizes different grants for the Fresh Fruit & Vegetable Program, they request separate billings to segregate costs. Our vendor confirmations showed annual costs from the Fresh Fruit and Produce vendors were billed appropriately by Sodexo compared to their records.
- “Other” costs in September 2017 related to a credit memo submitted as a negative amount, causing it to be reported as a charge.
  - Improperly billed credits totaling \$8,158, including a portion billed as labor costs, were credited to RCPS in the February 2019 invoice.
- The “Monthly Inventory Change” was an adjustment for changes in inventory on hand at the end of the month. We evaluated the inventory process in a separate objective later in this report.

#### Vendor Rebates & Discounts:

Federal regulations require food service management companies to credit all rebates and discounts to the school divisions at which the products are used. Incentives can take the form of signing bonuses, volume discounts, or rebates on specific purchases. Sodexo utilizes an internally developed database to allocate incentives to clients based on proportional monthly purchase volumes.

We verified that the incentives credited to RCPS for the months tested were consistent with the supporting allocation schedules provided by Sodexo from the aforementioned database. Our

reliance on the accuracy of the database rested on an attestation report issued by Cramer CPAs in 2013. Cramer’s auditors independently reviewed and tested Sodexo’s processes for allocating vendor incentives. The attestation was required as part of a \$20,000,000 settlement with the State of New York related to vendor rebates.

The Cramer report stated that rebates and discounts were appropriately allocated and equal to ~ 15% of product costs for the period reviewed.

Discounts credited to RCPS were noted to be substantially lower as follows:

	FY2017	FY2018
Gross Product Cost	3,973,548	3,793,193
Discounts	245,799	265,094
Discounts as a % of Product Costs	6.19%	6.96%

Sodexo District Management explained that opportunities to negotiate larger incentives are limited when working with smaller volumes and local vendors.

**Labor Costs**

<b>Operating Statement Line</b>	<b>FY2018 Costs</b>	<b>% of All Labor Costs</b>
Wages	2,183,544	76.30%
Benefits & Payroll Taxes	529,235	18.49%
Vacation Expense	129,621	4.53%

Sodexo uses KRONOS time management systems and ADP services to administer its payroll, including ~ 163 employees who provide services to students in Roanoke City Public Schools. Time worked is captured with time clocks at each school and processed in accordance with Sodexo policies. Employees are paid on a bi-weekly basis. All labor costs, including wages, payroll taxes, benefits, and processing fees are billed back to RCPS as part of the monthly invoice.

As noted earlier, we used September 2017 and April 2018 as a representative sample of monthly invoices for testing purposes. We performed extensive testing that included:

- Comparing Sodexo's payroll registers to the monthly invoices paid by RCPS.
- Analyzing variances in average daily hours worked and average hourly pay.
- Recalculating payroll taxes based on published rates.
- Recalculating payroll accruals and verifying reversing entries.

We found that invoices were consistent with the payroll registers. School-based staff worked on average 5.75 hours per day in both months. Pay rates averaged between \$9 and \$12 per hour in both months, with a slight increase in April. Payroll taxes included Social Security, Medicare, Federal and State unemployment, all of which we found to be consistent with published rates. Payroll processing fees were ~ \$550 per payroll run, which includes costs for ADP. We were unable to benchmark this cost due to the proprietary nature of pricing in this market space.

We selected a sample of 17 employees (~ 10%) for detail testing and performed the following for two bi-weekly payrolls in both September 2017 and April 2018:

- Recalculated earnings shown on the bi-weekly pay registers for each employee.
- Reviewed time cards for employees with overtime pay or significant variances in hours worked from the other pay periods reviewed.
- Reviewed rates of pay for employees with pay rate changes and confirmed they were correct by reviewing supporting HR records.

Based on the results of our work, we concluded that labor costs billed to RCPS by Sodexo were materially correct and in accordance with the contract.

### Controllable Costs

Sodexo bills the Division for materials and supplies, administrative costs such as background checks and training, and asset depreciation directly associated with RCPS operations. These costs totaled ~ \$638,522 for the year ending June 30, 2018. We audited the following line items taken from Sodexo's FY18 annual operating statement:

Operating Statement Line	FY2018 Costs (\$)	% of Controllable Costs
Paper / Plastic	423,532	66.33%
Small Equipment	50,060	7.84%
Cleaning Supplies	40,812	6.39%
Vehicle Expense	10,899	1.71%
Delivery / Fuel	14,293	2.24%
Special Services	5,412	0.85%
Miscellaneous	13,796	2.16%
Travel	6,242	0.98%
Promotions	3,697	0.58%
Office Supplies	21,169	3.32%
<b>Total Costs Tested:</b>	<b>589,912</b>	<b>92.40%</b>

As noted earlier, we confirmed ~ 97% of the annual purchases for FY2018 with the vendors who provided food and materials for RCPS food services. We also traced two months' expenditures from Sodexo's accounts payable records into the monthly operating reports and invoices. The results of this audit work provide sufficient support to conclude costs billed for materials and supplies were substantially correct.

Sodexo enters purchases of higher dollar equipment used in RCPS facilities into a fixed asset register and allocates the cost over the life of the equipment through depreciation charges. We reviewed Sodexo's detailed supporting schedules to identify the types of items capitalized, the reasonableness of associated costs and useful lives assigned, and the monthly allocations of depreciation. We noted that related costs, such as auto insurance, are incorporated into monthly billings for vehicle expenses.

We reviewed the nature of other direct costs such as training and travel expenses, and cell phone and email services provided to Roanoke-based Sodexo staff. These costs appeared appropriate based on our analytical review.

Overall, we concluded that controllable costs for FY18 were materially correct and billed in accordance with the terms and conditions of the contract.

### Non-controllable Costs

Non-controllable costs consist of management & administrative fees, insurance costs, amortization and other allocated corporate expenses:

	September 2017	April 2018	Total – FY18
Management & Admin Fees	64,728	52,453	579,750
Insurance	5,402	5,234	61,478
Amortization & Depreciation	4,717	3,818	42,578
Taxes, Licenses, & Fees	294	158	7,551
System Support	74	75	988
Totals:	<b>75,215</b>	<b>61,738</b>	<b>692,345</b>

We primarily focused on management and administrative fees and insurance costs. Our review of the fixed asset register and depreciation allocations under the controllable costs section included non-controllable allocations.

Management & Administrative Fees are based on the number of meal equivalents served (outlined in Objective #1). The contractual rates for FY18 were as follows:

- Management Fee = \$0.114 per meal equivalent
- Administrative Fee = \$0.124 per meal equivalent

Under Objective 3 of this report, we verified RCPS accurately reported meal counts based upon point-of-sale system data and meal rosters. We were then able to recalculate meal equivalents and the corresponding management and administrative fees to assess if the costs charged by Sodexo were in accordance with the contract.

Using the contractual rates and the verified meal counts, we confirmed the management and administrative fees billed for FY2018, including the months of September 2017 and April 2018, were materially correct and billed in accordance with the contract.

For insurance costs, the Division's contract with Sodexo stipulates, "charges for workers' compensation and general liability insurance (will be) based on the average manual rates for such insurance in the geographic area of the Premises." Based on our detailed review, we noted the following:

- Worker's Compensation Insurance costs were consistent with rates published by the National Council of Compensation Insurance, and the rates published on the Virginia State Corporation Commission's website for the restaurant industry (class code 9082).
- General Liability Insurance costs were based on an independent actuary's computations using loss rate data published by the Insurance Services Office (ISO). We verified that

Sodexo applied the actuarially determined monthly rate of \$3.53 per \$1,000 of gross sales correctly for the months tested.

We verified Sodexo's Certificate of Insurance included the required coverage specified by the contract, and that coverage amounts were consistent with those used in computing monthly rates.

Supporting reconciliations for both general liability and workers' compensation insurance agreed to the costs reported in the Client Revenue & Expense Detail for September 2017 and April 2018.

Overall, we conclude that non-controllable costs were materially correct and billed in accordance with the contract.

**End of Objective 2**



### **Objective 3: Meal Equivalent Reporting**

Were meal equivalents accurately reported?

#### **Overview**

The number of meals served is an important input for claiming grant funding from the USDA. As outlined in objective two, meal counts are also the basis for calculating management and administrative fees paid to Sodexo. Undercounting meals would cause RCPS to forgo USDA reimbursements to which the division is entitled. Inflating meal counts could result in questioned costs and the loss of grant funding, as well as overpayments to Sodexo.

Most meals are served in the school cafeteria where students pass through a serving line. Students enter their identification number into a point of sale (POS) system which brings up their account for the cashier. The cashier verifies the student has received a qualifying meal and completes the transaction. The POS system captures the necessary meal count information, including the type of meals served, the students who received meals, and the number of free, reduced, and paid meals.

RCPS pays for the POS system licenses and controls access to the system. The Director and Assistant Director of Food Services are the only persons with the capability to setup new users in the POS system. User rights are limited based on position and assigned responsibilities. The ability to edit or back date transactions is not granted to Sodexo employees. Student accounts can only be added to the POS system through a nightly interface with the Division's student information system, which is also controlled by RCPS employees.

A limited number of meals are provided outside of the cafeteria or at times when the POS system is not available. The names of students receiving these meals are recorded on a roster by the teacher or other school personnel who distributes the meals.

#### **Meal Count Testing**

We reviewed meal reimbursement claims from September 2017 and April 2018 to verify the claims were consistent with the POS system data and other meal count records. These two months account for 20.6% of the meals claimed in fiscal year 2018.

Meal Type	09/2017 Count	04/2018 Count	Combined	% of All Meals
Breakfast	113,545	87,634	201,179	35.2%
Lunch	196,295	156,853	353,148	61.8%
Supper – RCPS Sponsored	3,124	5,390	8,514	1.5%
Supper – YMCA Sponsored	915	1,038	1,953	.3%
<b>Meals Captured in Point of Sale System:</b>	<b>313,879</b>	<b>250,915</b>	<b>564,794</b>	<b>98.8%</b>
After School Snack	-	210	210	0.1%
Supper – RCPS Sponsored	550	2,247	2,797	0.5%
Supper – YMCA Sponsored	2,365	1,315	3,680	0.6%
<b>Meals Captured on Printed Rosters:</b>	<b>2,915</b>	<b>3,772</b>	<b>6,687</b>	<b>1.2%</b>

Meal reimbursement claims and those meals billed to the YMCA were consistent with the meal counts recorded in the POS system and printed rosters. Small differences in the number of meals claimed were immaterial to both the grant and the fees paid to Sodexo.

#### POS System User Access Controls Testing

There were 143 user accounts in the system as of October 2018 when we performed our review:

- 84 active accounts
- 59 inactive accounts

Inactive accounts are kept in the system to ensure no data is lost. The accounts are made inaccessible by selecting the “Prevent Client Login” setting in the user access setup.

We selected ten (10) active and five (5) inactive accounts for a detailed review of assigned access rights. Overall, our sample accounted for a little over 10% of all user accounts. The results of our review were positive, indicating that:

- Rights assigned to active accounts were appropriate to the roles and responsibilities of the users.
- Inactive accounts were appropriately marked to prevent logging into the system.

#### Annual Accountability Reviews

The Director and Assistant Director of Food Services perform required annual accountability reviews using a VDOE provided checklist at each school that serves meals. The checklist addresses meal counting and claiming processes as well as other aspects of cafeteria

operations, such as food preparation and storage. A corrective action plan must be developed for any deficiencies and a follow-up inspection must be conducted within 45 days to verify compliance. All cafeterias must be reviewed no later than February 1<sup>st</sup> of each school year.

We looked at each of the annual accountability reviews completed in the 2017/18 school year and confirmed that a checklist was on file for all 26 cafeterias in the division.

- 15 were completed by the February 1 deadline (58%), the other 11 were completed after the deadline.
- 8 cited deficiencies that required a follow-up review
  - o 5 follow ups were properly conducted within the 45 day limit
  - o 1 follow up was after the 45 day limit
  - o 2 follow up visits were not performed
- 2 cafeterias had minor issues with meal counts which were corrected in advance of the their follow-up review

Minor documentation inconsistencies were observed on 11 of the 26 checklists. While there are opportunities to improve the timeliness of reviews and follow-ups along with documentation, the annual accountability reviews are helping to ensure meal equivalent counts are correct and that other facets of cafeteria operations are satisfactorily performed.

Overall, appropriate controls are in place to help ensure meal count data is accurately reported to the USDA for reimbursement claims, and serves as a valid basis for Sodexo's administrative and management fees.

### **End of Objective 3**

### Objective 4: Inventory Management

Does Sodexo have appropriate inventory procedures in place for both purchased and USDA donated food?

#### Overview

Sodexo maintains a periodic inventory record of food and supplies. Deliveries of food and supplies are entered into the *Market Connection* inventory system when received. At the end of each month, school cafeteria employees take a physical inventory manually recording their counts on inventory sheets. Coordinators enter the counts into the inventory system. The inventory system computes the value of food and supplies used during the month, which is included in the monthly invoice for RCPS. The system does not enable management to account for inventory shrinkage and waste.

As the basis for billing food and materials costs to the Division, we considered the inventory process to be a key control for ensuring accurate billing and for controlling costs. On October 30, 2018, we visited three schools to verify that inventories were being completed as management intended:

- Virginia Heights Elementary
- Woodrow Wilson Middle School
- Patrick Henry High School

We noted that counts are performed by two people, one counting and the other recording the count on the inventory sheets. Inventory printouts used to record the counts do not show the expected quantities, which helps ensure a more accurate count of items actually on-hand.

We selected 20 items at each school and re-performed the count to verify accuracy. To ensure donated USDA products were clearly marked and kept separate from purchased goods, as required by USDA regulations, we asked Cafeteria Managers to walk us through all storage areas and to identify USDA products.

We concluded that inventories were generally completed in accordance with management's expectations and correctly entered into the *Market Connection System* by Coordinators. We noted a modest degree of error in the counts we tested, as follows:

School *	Total October Inventory	Test Variance (\$)	Test Variance (%)	Extrapolated Variance
VA Heights	\$11,414.92	\$ (122.54)	(10.93)%	\$(1,247.73)
Woodrow Wilson	12,238.88	39.87	4.03%	492.79
Patrick Henry	20,173.66	169.65	7.98%	1,610.15
<b>Total</b>	<b>43,827.46</b>	<b>86.98</b>	<b>2.05%</b>	<b>855.21</b>

\* Figures include USDA and Purchased Good inventories – USDA commodities are priced at market value but are not billed since Sodexo incurs no costs for donated goods.

Errors in recording quantities can occur due to misreading of the unit of measure, overlooking an item, or miscommunication between counter and recorder. We considered the impact of such errors on operations and billing to be minimal based on Sodexo's periodic inventory approach. Errors are expected to wash out assuming an earnest effort to correctly count inventories each subsequent month.

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### ***USDA Commodity Inventory***

Federal regulations require RCPS to confirm at least annually that Sodexo appropriately credited the Division for the value of donated foods received and used. This information was reported on Sodexo's annual operating statement for the year ended June 30, 2018. Upon review, we noted that Sodexo had inaccurately reported commodity activity for FY18 as follows:

	Estimated Value	Sodexo Statement	Variance
<b>Commodity Inventory Received</b>	591,500	103,433	488,066
<b>Commodity Inventory Used</b>	589,559	556,773	32,785
<b>Commodity Inventory Received less Used</b>	1,940	9,515	(7,575)

We looked back at Sodexo's monthly operating statements and found that the value of donated food for the year was almost entirely reversed out of the April statement. While this is essentially a paper error and had no effect on the cost of goods billed to the school division, it is indicative of a data reliability issue. This should have been investigated promptly and the cause determined to help ensure the integrity of Sodexo's future operating statements.

The Food Services department had noticed the misstated commodities numbers, but did not report the issue to Sodexo. The Director stated that the department monitors commodity deliveries reported by the USDA's third party distributor against delivery slips forwarded by Cafeteria Managers as deliveries are received at the schools.

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*Inventory Consumption Analysis*

As noted previously, Sodexo uses a periodic inventory system. The quantity and cost of each food and supply item delivered to a school are recorded in the inventory system. When the food and supplies are taken out of inventory, no entry is recorded. The system imputes the cost of goods sold based on the quantity of items on hand at the end of the month. Losses due to theft, spoilage and waste are not identifiable in this type of system.

Under the cost-reimbursable contract with Sodexo, any costs associated with poor inventory controls are borne by the Division. Food is inherently at risk for pilferage, overproduction, and spoilage. A periodic inventory system is not designed to prevent or detect risks of this nature. Other compensating controls are needed to reduce the risks of losses from misappropriation and waste.

During the course of our audit, we did not identify any compensating controls related to inventory.

**End of Objective 4**

**SUMMARY OF MANAGEMENT ACTION PLANS**

**Management Action Plan – Internal Audits**

Monthly Monitoring:

RCPS will request the following documents to be included with the Monthly Operating Statement:

- Client Revenue and Expense Detail
- Ending Inventory Report.

Meal Equivalents will be recalculated to Management and Administrative Fees utilizing testing spreadsheet provided.

Quarterly Monitoring:

RCPS will request the following documents to be provided by Sodexo quarterly:

- AP Detail
- Depreciation Schedule.

The documents will be reviewed for significant/unusual items including moderate and high risk components: journal entries, allocations, and other.

Alternating quarters, RCPS will randomly review pay roll registers, observe inventory counting process, review Primero Edge reports (production records), and Vendor Discounts.

Annual Monitoring:

RCPS will request vendor expenditure summary from full A/P detail from Sodexo. In addition, RCPS will obtain independent external sales information from vendor contacts and compare totals, investigate any significant variances through analysis of vendor support and Sodexo’s A/P detail.

Assigned To	Target Date
Ellen Craddock, Director of Food and Nutrition	09/01/2019

**Management Action Plan – Sodexo Budget**

RCPS Food and Nutrition will follow-up on Article 2.4 of the Contract for School Food Programs Management Services-RFP by sending a formal written request for the next fiscal year’s budget. The request will be sent allowing 30 days’ notice to the General Manager of SodexoMAGIC for RCPS of the December 15<sup>th</sup> deadline. The District Manager of SodexoMAGIC will be copied in correspondence.

In the formal written correspondence aforementioned to the General Manager and District Manager of SodexoMAGIC, RCPS will request Sodexo’s budget detail to include:

- Definitions of what each line item expenditure represents / includes.
- Dollar (\$) and percent (%) change from prior year budget and prior year actual.
- Explanations of the basis for significant changes in individual line items from prior year, for example; percentage employee raises and percentage increases in healthcare costs
- Key assumptions that if not met could have significant impact.

<p>- Multi-year projections of equipment replacement needs.</p> <p>If RCPS does not receive Sodexo’s budget by the December 15<sup>th</sup> deadline, then a formal letter will be sent to the General Manager and District Manager of SodexoMAGIC warning payment for December services will not be approved until the contracted scope of work under Article 2.4 for December is completed.</p>	
<b>Assigned To</b>	<b>Target Date</b>
Ellen Craddock, Director of Food and Nutrition.	12/15/2018

<p><b>Management Action Plan – Advisory Board</b></p> <p><u>Student Promotion Coordinator Annual Selection</u></p> <p>A Student Promotion Coordinator will be identified with the assistance of the high school principals at William Fleming High School and Patrick Henry High School annually to participate on the School Board’s Food Service Committee/Advisory Board and provide input to school menus during quarterly Food Service Committee meetings.</p> <p><u>Student Promotion Coordinators approved as Food Service Committee/Advisory Board Members</u></p> <p>Names of Student Promotion Coordinators for William Fleming High School and Patrick Henry High School will be submitted for approval to serve on the School Board Food Service Committee no later than the November School Board meeting’s agenda.</p> <p><u>Student Feedback on Menu Options</u></p> <p>Sodexo will provide cycle menus at the quarterly Food Service Committee meetings for students, principals, and parents to provide feedback. New promotional menu items may be presented for taste testing.</p> <p><u>Food Service Committee / Advisory Board Structure</u></p> <p>The Director of Food and Nutrition in coordination with the Deputy Superintendent and School Board Committee Chairman will establish the structure of the Food Service committee to include: purpose, goals, constituent membership, support staff and frequency of meetings.</p>	
<b>Assigned To</b>	<b>Target Date</b>
Ellen Craddock, Director of Food and Nutrition Cynthia Poulton, School Board Clerk SodexoMAGIC General Manager	January 2018 committee meeting



**Management Action Plan – On-Site Accountability Reviews**

On-site Accountability Review

RCPS will prepare a checklist of school reviews to complete for the Director and Assistant Director by September 1<sup>st</sup> of each year. Each monitor will be assigned 13 sites to review for lunch and 6 or 7 sites for breakfast. The monitors will set a goal to complete one lunch review per week beginning the week of September 1<sup>st</sup> and ending the week prior to Winter Break. A goal will be set to review a breakfast program every other week beginning the week of September 1<sup>st</sup> and ending the week prior to Winter Break.

Required Follow-up Visits

RCPS will send a letter to the Sodexo GM and Supervisor of sites requiring a 45-day follow-up. The Director and Assistant Director will set a reminder in Microsoft Outlook for the date to follow-up by.

Quality Control

The Director and Assistant Director will review each other’s On-Site Accountability Reviews upon return from Winter Break for accuracy, completeness, then initial and date each document.

Assigned To	Target Date
Ellen Craddock, Director of Food and Nutrition	1/6/2020

**Management Action Plan –Inventory Monitoring**

Purchased Food and Supply Inventory Monitoring

Sodexo will provide a summary of Purchased Food and Supplies for each school at the end of each month. RCPS will compile information provided into a spreadsheet to compare inventory by school. The Sodexo GM and Food Service Director will review trends of comparative schools within the month and changes month to month and address any issues or concerns noted.

Commodity Monitoring

Sodexo will provide copies of Commodity Inventory Extension by Location for each site in addition to a Commodity Summary report at the end of each month. The Sodexo GM and Food Service Director will review trends of comparative schools within the month and changes month to month and address any issues or concerns noted.

Monthly Food Cost Monitoring

RCPS can track monthly food cost as a percentage of total expenditures and as cost per meal equivalent. The Sodexo GM and Food Service Director will review trends of comparative schools within the month and changes month to month and address any issues or concerns noted.

Assigned To	Target Date
Ellen Craddock, Director of Food and Nutrition	4/1/2019

<b>Management Action Plan –Commodity Inventory Reconciliation</b>	
<p>RCPS will compare records of commodity goods received with those reported as received by Sodexo. Month-ending inventory reports will be obtained from Sodexo to calculate inventory consumption in the month. RCPS will compare the calculated consumption totals to those reported by Sodexo in their monthly operating statement. Any variance will be recorded and discussed with Sodexo management.</p>	
<b>Assigned To</b>	<b>Target Date</b>
Ellen Craddock, Director of Food and Nutrition	4/1/2019

**MANAGEMENT COMMENTS**

None provided

**ACKNOWLEDGEMENTS**

We would like to thank the Director and Assistant Director of Food Services, along with Sodexo's local management team for their assistance with this audit. We would also like to thank the suppliers who responded to confirmation requests for their willingness to provide supporting records. Finally, we wish to thank the VDOE's Office of School Nutrition for providing meal count and financial data for comparable localities used in our benchmarking analysis procedures.



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Brian J. Pendleton, CPA  
Senior Auditor



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Drew Harmon, CPA, CIA  
Municipal Auditor