

**UNITED STATES DEPARTMENT OF AGRICULTURE**

**None FOOD FOR PROGRESS PROGRAM**  
**None SECTION 416(b) PROGRAM**

**I. PROGRAM OBJECTIVES**

The U.S. Department of Agriculture (USDA) donates agricultural commodities for use in carrying out assistance programs in developing countries and friendly countries. Such countries are often emerging democracies that have made a commitment to introduce or expand private enterprise elements into the agricultural sectors of their economies.

**II. PROGRAM PROCEDURES****General Overview**

The Food for Progress Program and the Section 416(b) Program (Foreign Food Aid Donation Programs) are Commodity Credit Corporation (CCC) programs. CCC implements these programs through personnel of the Foreign Agricultural Service (FAS) and Farm Service Agency (FSA). The CCC, a wholly-owned government corporation within the USDA, may acquire agricultural commodities under various surplus removal and agricultural price support programs and make them available for various domestic and foreign food assistance programs. Under the Food for Progress Act of 1985, CCC may purchase commodities from the market for donation overseas.

Recipients under the Foreign Food Aid Donation Programs are known collectively as Cooperating Sponsors. The CCC makes commodities available to the Cooperating Sponsors for use in the operation of charitable and economic development activities in eligible foreign countries. Cooperating Sponsors may be foreign governments or private entities including non-profit organizations located in the United States but operating programs overseas which are registered with the United States Agency for International Development (7 CFR section 1499.3).

The two programs have different criteria for determining what is an eligible foreign country.

*Food for Progress Program* - Commodities made available under this program, regardless of funding source, must be donated for use in developing countries and emerging democracies that have made commitments to introduce or expand free enterprise elements in their agricultural economies.

*Section 416(b) Program* - Section 416(b) of the Agricultural Act of 1949 authorizes the donation of CCC-owned commodities in excess of domestic program requirements to carry out food assistance programs in developing and friendly countries.

## **Program Operation**

### *General*

A Cooperating Sponsor must file a Plan of Operation with the CCC under the Section 416(b) Program. The CCC is also authorized to require such a plan under the Food for Progress Program (7 CFR section 1499.5). This Plan of Operation becomes part of an agreement between the CCC and the Cooperating Sponsor. The plan or agreement stipulates, among other things, the nature of the project the sponsor proposes to operate, the country in which such operations will take place, the types and quantities of commodities needed, the purpose for which the commodities will be used, and the use of either direct distribution or monetization of commodities. The Cooperating Sponsor is responsible for fulfilling the reporting requirements concerning logistics, monetization, and quarterly financial reports.

### *Direct Distribution*

A direct distribution by the Cooperating Sponsor involves the distribution of donated commodities directly to individuals or charitable institutions in the host country referred to as Recipient Agencies (e.g., hospitals, schools, kindergartens, orphanages, homes for the elderly). These Recipient Agencies then use the commodities in serving their clientele.

### *Recipient Agencies*

A Cooperating Sponsor must enter into an agreement with a Recipient Agency prior to the transfer of any commodities, sales proceeds, or program income to the Recipient Agency. The agreement must require the Recipient Agency to compensate the Cooperating Sponsor for any agricultural commodities or other assets generated by the program that are not used for purposes expressly provided for in the agreement, or that are lost, damaged, or misused as the result of the Recipient Agency's failure to exercise reasonable care.

### *Monetization*

A monetization agreement authorizes the Cooperating Sponsor to sell the commodities in the applicable foreign country and use the sales proceeds to support its programmatic activities in accordance with the signed agreement. To the maximum extent possible, the Cooperating Sponsor is expected to conduct the sale of commodities through the private sector of the host country's economy. A Cooperating Sponsor's agreement with the CCC may also provide for bartering commodities in exchange for goods and services to support program operations.

In addition to commodities, the CCC's agreement with the Cooperating Sponsor may provide the Cooperating Sponsor cash assistance to fund program administrative and operational expenses. Program regulations also authorize cash advances for this purpose. Such cash awards may be made only after approval of a program operating budget submitted by the Cooperating Sponsor.

## Source of Governing Requirements

Commodity donations are authorized by the Food for Progress Act of 1985 (7 USC 1736o) (Food for Progress Program) and Section 416(b) of the Agricultural Act of 1949 (7 USC 1431(b)) (Section 416(b) Program). Implementing regulations are found at 7 CFR part 1499.

## Availability of Other Program Information

For more information, contact the Director, CCC Program Administration Division, FAS, USDA at Stop 1031, 1400 Independence Avenue, S.W., Washington, D.C. 20250-1031. Contacts may also be made through: (202) 720-4221 (voice); (202) 690-0251 (fax); or info@fas.usda.gov (E-mail).

## III. COMPLIANCE REQUIREMENTS

**In developing the audit procedures to test compliance with the requirements for a Federal program, the auditor should first look to Part 2, Matrix of Compliance Requirements, to identify which of the 14 types of compliance requirements described in Part 3 are applicable and then look to Parts 3 and 4 for the details of the requirements.**

### A. Activities Allowed or Unallowed

#### 1. *Use of Funds*

The Plan of Operation and agreement set forth the description of the activities for which commodities, monetized proceeds, or program income shall be used.

Except as approved in advance by CCC, the Cooperating Sponsor shall ordinarily bear all costs incurred subsequent to CCC's delivery of commodities at U.S. ports or intermodal points (7 CFR section 1499.7(d)).

With prior written approval from CCC, the Cooperating Sponsor may use CCC funds for administrative expenses under the Food for Progress Program. Administrative expenses include expenses incurred for the purchase of goods and services directly related to program administration and monitoring of distribution and monetization operations (7 CFR section 1499.7(b)(3)).

#### 2. *Use of Commodities and Monetization Proceeds*

A Cooperating Sponsor must use USDA commodities furnished under the Foreign Food Aid Donation Programs, and proceeds from the sale of such commodities if applicable, for purposes expressly provided for in its agreement with the CCC (7 CFR sections 1499.10(a) and 1499.12(d)).

Agreements with Cooperating Sponsors implementing Section 416(b) projects may provide for the use of proceeds from monetization operations to fund administrative expenses (7 USC 1431(b)(7)(F)).

## **C. Cash Management**

### *1. Cash Advances From the CCC*

A Cooperating Sponsor may request an advance of up to 85 percent of the amount of an approved program operating budget. Cash advances furnished by the CCC must be deposited in interest bearing accounts. Any interest earned on such advances must be used for the same purposes as the cash advances themselves (7 CFR sections 1499.7(f) and (g)).

### *2. Commodity Monetization Proceeds*

A Cooperating Sponsor must deposit all proceeds from the sale of USDA-donated commodities under monetization agreements into interest bearing accounts. Exceptions are permitted where this practice is prohibited by local law or custom of the importing country or the CCC determines that enforcing the requirement would impose an undue burden on the sponsor (7 CFR section 1499.12(c)).

## **F. Equipment and Real Property Management**

To the extent required by the program agreement, a Cooperating Sponsor must furnish the CCC and FAS with inventory lists of equipment and real property acquired with proceeds from the sale of donated commodities, interest, and other program income (OMB No. 0551-0035). When such assets are no longer needed for program purposes, the sponsor must dispose of them in accordance with 7 CFR section 1499.12(g).

## **H. Period of Availability of Federal Funds**

Any portion of a cash advance not obligated by the Cooperating Sponsor within 180 days of receipt, and any related interest, must be refunded to the CCC within 30 days after the Cooperating Sponsor's obligational authority over the funds has expired (7 CFR section 1499.7(h)).

CCC will not pay any cost incurred by the Cooperating Sponsor prior to the date of the program agreement (7 CFR section 1499.7(c)).

## **I. Procurement and Suspension and Debarment**

A Cooperating Sponsor must follow commercially reasonable practices in procuring goods and services and when engaging in construction activity in accordance with its agreement with the CCC (7 CFR section 1499.12(f)).

## **J. Program Income**

Program income includes interest on sale proceeds and money received by the Cooperating Sponsor, other than monetization proceeds, as a result of carrying out approved activities (7 CFR section 1499.1). A Cooperating Sponsor must use program

income for program purposes identified in its agreement with the CCC (7 CFR section 1499.5).

## **L. Reporting**

### **1. Financial Reporting**

- a. SF-269, *Financial Status Report* - Not Applicable
- b. SF-270, *Request for Advance or Reimbursement* - Not Applicable
- c. SF-271 - *Outlay Report and Request for Reimbursement for Construction Programs* - Not Applicable
- d. SF-272 - *Federal Cash Transactions Report* - Not Applicable
- e. *Financial Statement (OMB No. 0551-0035)* - Any Cooperating Sponsor that receives an advance of CCC funds must file quarterly financial statements with the CCC.

#### *Key Line Items:*

- (1) Cash on hand at beginning of the quarter.
- (2) CCC advances received during the quarter.
- (3) Interest earned during the quarter.
- (4) Expenditures for administrative and Internal Transportation, Storage, and Handling (ITSH) costs during the quarter. Both categories of cost must be subdivided into sub-categories identified in instructions issued by the FAS.
- (5) Cash on hand at the end of the quarter.

### **2. Performance Reporting**

- a. CCC Form 620, *Logistics Report (OMB No. 0551-0035)* - A Cooperating Sponsor must submit this report to the FAS semiannually for each agreement. If commodities are distributed directly, the sponsor must continue submitting reports until all commodities made available under the agreement have been distributed. In the following detail, quantities of commodities are reported in terms of net metric tons (NMT) unless otherwise specified (7 CFR section 1499.16(c)(1)).

*Key Line Items* - The following line items contain critical information:

- (1) *Commodity Delivery Table* - The following data relating to **shipping** of each commodity provided for in the agreement:
    - (a) *Amount received at port.*
    - (b) *Ocean losses/damages.*
    - (c) *Amount received at warehouse.*
    - (d) *Inland losses/damages.*
  - (2) *Freight Charges* - The dollar amount of claims for a reduction or recovery of freight charges in both local currency and U.S. dollar equivalents. Claims generated by the ocean and inland portions of the shipment should be separately identified.
  - (3) *Warehouse Losses* - The following data relating to **storage** of each commodity provided for in the agreement:
    - (a) *Warehouse losses/damages.*
    - (b) *Balance available for distribution.*
  - (4) *Direct Distribution* - The following data relating to **direct distribution** of each commodity provided for in the agreement:
    - (a) *Amount distributed.*
    - (b) *Distribution losses/damages.*
    - (c) *Type of institution reached and number of institutions reached.*
    - (d) *Number of benefiting individuals.*
  - (5) *Warehouse Inventory Status* - The warehouse inventory status of each commodity provided for in the agreement: beginning inventory, total received in warehouse, total dispatched from warehouse, warehouse losses, and ending inventory.
- b. CCC Form 621, *Monetization Report (OMB No. 0551-0035)* - A Cooperating Sponsor must submit this report to the FAS semiannually for each agreement that provides for monetization of the commodities. Reports are required until all the commodities have been sold and the proceeds disbursed for authorized purposes. If a monetization project involves a revolving loan program, current FAS policy requires the

Cooperating Sponsor to submit reports only through repayment of the first loan cycle.

Methods a Cooperating Sponsor may use to determine prevailing local market prices for monetization purposes include, but are not limited to, soliciting sealed bids, using public auctions, involving commodity exchanges, or obtaining written statements from the agricultural attache or minister for foreign agricultural affairs in the host country. Contact information for all FAS offices overseas is available on the Internet at [http://www.fas.usda.gov/scripts/w/fasfield/ovs\\_directory\\_search.asp](http://www.fas.usda.gov/scripts/w/fasfield/ovs_directory_search.asp).

*Key Line Items* - The following line items contain critical information:

*Part I - Sales:*

For each commodity provided for in the agreement: the amount sold, the price per MT (metric ton), exchange rate, proceeds generated in LC (local currency), and proceeds generated in USD (U.S. dollar equivalent).

*Part II - Barter:*

For each commodity used in barter exchanges: the type and amount bartered, the commodity/service received, and the domestic price on transaction date for commodity bartered and commodity/service received.

*Part III - Deposits to Special Funds Account:*

The following classes of funds deposited, both in local currency and in the equivalent number of U.S. dollars: sales of commodities, interest, other program income.

*Part IV - Disbursements From Special Funds Account:*

The amount of each disbursement, in both local currency and U.S. dollars, and a brief statement of the use of funds.

*Part V - Balance of Special Funds Accounts:*

Beginning and ending balances of special fund accounts, both in local currency and in U.S. dollars.

**3. Special Reporting - Not Applicable**

## N. Special Tests and Provisions

### 1. Recipient Agencies

**Compliance Requirement** - The Plan of Operation is required to describe the Recipient Agencies that will be involved in the program and a description of each Recipient Agency's capability to perform its responsibilities (7 CFR section 1499.5(a)(3)). A Recipient Agency is defined as an entity located in the foreign country that receives commodities or commodity sale proceeds from a Cooperating Sponsor for the purpose of implementing activities (7 CFR section 1499.1).

The Cooperating Sponsor must enter into a written agreement with a Recipient Agency before transferring USDA commodities, monetization proceeds, or other program income to that entity. Such an agreement must require the Recipient Agency to pay to the Cooperating Sponsor the value of any commodities provided by USDA, sales proceeds, or other program income not used for purposes expressly permitted under the Cooperating Sponsor's own agreement with the CCC; or that are lost, damaged, or misused as the result of the Recipient Agency's failure to exercise reasonable care (7 CFR section 1499.11(a)).

The Cooperating Sponsor must ensure that the activities of any Recipient Agency that receives \$25,000 or more in commodities or commodity sales proceeds are subjected to on-site inspection. The Cooperating Sponsor may meet this requirement by relying upon independent audits of the Recipient Agencies or by conducting its own on-site reviews (7 CFR section 1499.17).

**Audit Objective** - Determine whether (1) the Cooperating Sponsor entered into written agreements with the Recipient Agencies, (2) the use of the Recipient Agencies was consistent with the Plan of Operation, and (3) the Cooperating Sponsor monitored the activities of Recipient Agencies to ensure proper performance of assigned activities and use of commodities, monetized proceeds, and program income.

#### **Suggested Audit Procedures**

Select a sample of Recipient Agencies and ascertain if:

- a. The Cooperating Sponsor entered into a written agreement with the Recipient Agency.
- b. The Cooperating Sponsor's use of the Recipient Agency was consistent with the Plan of Operation.
- c. The Cooperating Sponsor appropriately monitored the activities of the Recipient Agency to ensure proper performance of assigned activities and use of commodities, monetized proceeds, and program income.

## UNITED STATES DEPARTMENT OF AGRICULTURE

### CFDA 10.500 COOPERATIVE EXTENSION SERVICE

#### I. PROGRAM OBJECTIVES

The Cooperative State Research, Education, and Extension Service (CSREES) provides formula grant funds to the 1862 land-grant institutions and the 1890 land-grant institutions for cooperative agricultural extension work which consists of the development of practical applications of research knowledge and practical demonstrations of existing or improved practices or technologies in agriculture, uses of solar energy with respect to agriculture, home economics, and rural energy, and related subjects to persons not attending or resident in colleges.

#### II. PROGRAM PROCEDURES

The First Morrill Act of 1862 provided for the establishment of the 1862 land-grant institutions which are located in the 50 States, the District of Columbia, the Commonwealth of Puerto Rico, and the insular areas of American Samoa, Guam, Micronesia, Northern Marianas, and the Virgin Islands. The Second Morrill Act of 1890 provided for the support of the 1890 land-grant institutions, including Tuskegee University and West Virginia State University, which are located in 16 States.

The 1862 land-grant institutions receive formula grant funds for cooperative extension work under sections 3(b) and (c) of the Smith-Lever Act and the 1890 land-grant institutions, including Tuskegee University and West Virginia State University, receive formula grant funds for cooperative extension work under section 1444 of the National Agricultural Research, Extension, and Teaching Policy Act of 1977 (NARETPA). The only exception is the District of Columbia, which receives extension funds under the District of Columbia Public Postsecondary Education Reorganization Act, Pub. L. 93-471, as opposed to the Smith-Lever Act.

Funds are allocated to the land-grant institutions based on specified formulas, and these funds are made available to the land-grant institutions at the beginning of each quarter through the Department of Health and Human Services' Payment Management System (DHHS-PMS). These formulas are based on the farm and rural populations of each state and include an equal portion distributed to all eligible institutions. These funds support the activities commonly referred to as "base programs."

Formula funds are also provided to the 1862 land-grant institutions under section 3(d) of the Smith-Lever Act for the expanded food and nutrition education program which is authorized under section 1425 of NARETPA, and these funds are made available to the 1862 land-grant institutions in the 50 States, the Commonwealth of Puerto Rico, and the insular areas of American Samoa, Guam, Micronesia, Northern Marianas, and the Virgin Islands. To enable low-income individuals and families to engage in nutritionally sound food purchasing and preparation practices, the expanded food and nutrition education program provides for employment and training of professional and paraprofessional aides to engage in direct nutrition education of low-income families and in other appropriate nutrition education programs. To the maximum extent practicable, program aides are hired from the indigenous target population.

The 1862 and the 1890 land-grant institutions are required to submit a 5-Year Plan of Work which describes the extension programs that they intend to administer for the period from October 1, 1999, through September 30, 2004 (7 USC 344 and 3221). A 2-Year Plan of Work Update only for fiscal year (FY) 2005 and FY 2006, is required instead of submitting a new 5-Year Plan of Work for FY 2005-FY 2009 (Revisions to the Guidelines for State Plans of Work for the Agricultural Research and Extension Formula Funds, 69 Federal Register (FR) 6244-48, February 10, 2004).

### **Source of Governing Requirements**

The laws governing this program are codified at 7 USC 301-349, 3221, 3222, 3222d, and 3319.

### **Availability of Other Program Information**

Additional program information is available from the CSREES site on the Internet at <http://www.csrees.usda.gov>.

## **III. COMPLIANCE REQUIREMENTS**

**In developing the audit procedures to test compliance with the requirements for a Federal program, the auditor should first look to Part 2, Matrix of Compliance Requirements, to identify which of the 14 types of compliance requirements described in Part 3 are applicable and then look to Parts 3 and 4 for the details of the requirements.**

### **A. Activities Allowed or Unallowed**

1. Formula grant funds may be spent only for the furtherance of cooperative extension work and according to the 5-Year Plan of Work or 2-Year Plan of Work Update approved by CSREES (7 USC 344 and 3221(d)). The Guidelines for the State Plans of Work for Agricultural Research and Extension Formula Funds were published in the *Federal Register* on July 1, 1999 (64 FR 35910-35919). The 5-Year Plan of Work for fiscal year (FY) 2000 through FY 2004 was due July 15, 1999. This 5-Year Plan of Work may be integrated with the research component of the land-grant institution which is funded under the Hatch Act, and/or the 5-Year Plan of Work may be a joint plan between an 1862 land-grant institution and an 1890 land-grant institution if they are both located in the same State (64 FR 35916). Guidelines for the 2-Year Plan of Work Update were published in the *Federal Register* on February 10, 2004 (69 FR 6244-48). The 2-Year Plan of Work Update extends coverage of the original 5-Year Plan of Work to include FY 2005 through FY 2006 and was due April 1, 2004. The 2-Year Plan of Work Update should continue to be based on the original national goals established in the FY 2000 – FY 2004 Plan of Work.
2. No portion of Smith-Lever Act funds and section 1444 funds of NARETPA may be applied directly or indirectly “to the purchase, erection, preservation or repair of any building or buildings, or the purchase or rental of land” (7 USC 345 and 3221(e)).

3. No portion of Smith-Lever Act funds and section 1444 funds under NARETPA may be applied directly or indirectly in college course teaching or lectures in college (7 USC 345 and 3221(e)).

## **B. Allowable Costs/Cost Principles**

1. *Indirect Costs* - No indirect costs or tuition remission may be charged against the formula grant funds authorized under the Smith-Lever Act or under section 1444 of NARETPA (7 USC 3319).
2. *Retirement Contributions* - Retirement and pension contributions paid from grant funds for individuals whose salaries are paid in whole or in part with grant funds are capped at 5 percent. The deposits and contributions of Federal origin must be at least equaled by the grantee (7 USC 331).

## **G. Matching, Level of Effort, Earmarking**

### **1. Matching**

- a. *1862 Land-Grant Institutions in the 50 States* - All formula funds provided to the 1862 land-grant institutions in the 50 States under sections 3(b) and (c) of the Smith-Lever Act must be 100 percent matched. In-kind contributions are not allowed as match for formula funds authorized under sections 3(b) and (c) of the Smith-Lever Act (7 USC 343(e)). Funds provided under section 3(d) of the Smith-Lever Act for the expanded food and nutrition education program (EFNEP) do not require any matching contributions (7 USC 3175).
- b. *1862 Land-Grant Institution in the District of Columbia* - All allocations made to the 1862 land-grant institution in the District of Columbia under the District of Columbia Public Postsecondary Education Reorganization Act, Pub. L. 93-471, must be 100 percent matched. In-kind contributions are not allowed as match for formula funds (Pub. L. 93-471, Section 208(c)).
- c. *1862 Land-Grant Institutions in the Commonwealth of Puerto Rico and the insular areas of American Samoa, Guam, Micronesia, Northern Marianas, and the Virgin Islands* - The Commonwealth of Puerto Rico and the insular areas must meet a 50 percent matching requirement of the Federal formula funds beginning in FY 2003 (7 USC 343(e)(4) and 7 USC 301 (note)). The Secretary of Agriculture may waive the matching funds requirement for any fiscal year if the Secretary determines that the government of the insular area will be unlikely to meet the matching requirement for the fiscal year (7 USC 343(e)(4)). "Matching funds" means cash contributions and excludes in-kind matching contributions. Matching funds must be used to support research and extension activities as identified in the approved 5-Year Plan of Work and the 2-Year Plan of

Work Update or for approved qualifying educational activities (7 USC 343(e); 7 CFR part 3419).

- d. *1890 Land-Grant Institutions, including Tuskegee University and West Virginia State University* - In FY 2003, the matching requirement is 60 percent; in FY 2004, 70 percent; in FY 2005, 80 percent; in FY 2006, 90 percent; and in FY 2007 and thereafter, 100 percent. These land-grant institutions may apply for a waiver of the matching funds requirement in excess of 50 percent for any fiscal year. "Matching funds" means cash contributions and excludes in-kind matching contributions. Matching funds must be used to support research and extension activities as identified in the approved 5-Year Plan of Work and the 2-Year Plan of Work Update or for approved qualifying educational activities. Matching funds must be available in the same Federal fiscal year as the Federal funds. 1890 Land-Grant Institutions, including Tuskegee University and West Virginia State University, may carryover matching funds from one fiscal year to the following fiscal year (7 USC 3222d and 7 CFR part 3419).

2. **Level of Effort** - Not Applicable

3. **Earmarking** - Not Applicable

## H. **Period of Availability of Federal Funds**

Smith-Lever Act formula funds distributed to the 1862 land-grant institutions may be carried forward five years from the year allocated. For Section 1444 of NARETPA funds allocated to the 1890 land-grant institutions, including Tuskegee University and West Virginia State University, no more than 20 percent of the funds received in any fiscal year may be carried forward to the succeeding fiscal year (7 USC 3221(a)).

## L. **Reporting**

### 1. **Financial Reporting**

- a. SF-269, *Financial Status Report* - This report is due from the 1862 land-grant institutions by April 1 (7 USC 344(b)) and from the 1890 land-grant institutions, including Tuskegee University and West Virginia State University, by December 1 (7 USC 3221(d)).
- b. SF-270, *Request for Advance or Reimbursement* - Not Applicable
- c. SF-271, *Outlay Report and Request for Reimbursement for Construction Programs* - Not Applicable
- d. SF-272, *Federal Cash Transactions Report* - Payments under this program are made by the HHS Payment Management System. Reporting

equivalent to the SF-272 is accomplished through the Payment Management System and is evidenced by the PSC-272 series of reports.

2. **Performance Reporting** - Not Applicable
3. **Special Reporting** - Not Applicable

**UNITED STATES DEPARTMENT OF AGRICULTURE****CFDA 10.551 FOOD STAMPS****CFDA 10.561 STATE ADMINISTRATIVE MATCHING GRANTS FOR FOOD STAMP PROGRAM****I. PROGRAM OBJECTIVES**

The objective of the Food Stamp Program is to help low-income households buy the food they need for good health.

**II. PROGRAM PROCEDURES****Administration**

The U.S. Department of Agriculture (USDA), Food and Nutrition Service (FNS) administers the Food Stamp Program in cooperation with State and local governments.

State welfare agencies (or county welfare agencies under the oversight of the State government) certify eligibility and provide benefits to households. FNS authorizes, monitors, and investigates stores that redeem benefits, provides funding for State administration and benefits, and oversees the operation of State welfare agencies to ensure compliance with Federal laws and regulations.

**Federal Funding of Benefits and State Administrative Costs**

The Federal Government pays 100 percent of the value of Food Stamp Program benefits and generally reimburses States for 50 percent of their costs to administer the program (7 CFR section 277.4(b)), except for those functions listed in III G.1., Matching. The Food Stamp Program's authorizing statute places no cap on the amount of funds available to reimburse States at the 50 percent rate for allowable administrative expenses. No reimbursement is allowed for State expenditures for activities undertaken as a condition of settlement of quality control claims against the State for low payment accuracy.

**Certification**

Eligibility for food stamps is based primarily on income and resources. Although welfare reform and subsequent legislation increase State design options that can affect benefits for recipients, a key feature of the program is its status as an entitlement program with standardized eligibility and benefits.

*Assessing Need*

Households generally cannot exceed a gross income eligibility standard set at 130 percent of the Federal poverty standard (7 CFR section 273.9(a)(1)). Households also cannot exceed a net income standard, which is set at 100 percent of the Federal poverty standard (7 CFR section 273.9(a)(2)). The net income standard allows specified deductions from gross income, e.g., a standard deduction and deductions for medical expenses (elderly and disabled only), excess shelter costs, and work expenses. Non-financial eligibility criteria include: age, school status,

citizenship/legal immigration status, residency, household composition, work requirements, and disability status. Some non-citizens are ineligible to participate in the program (7 USC 2015(f)). Able-bodied adults without dependents are subject to a time limit for receiving benefits if certain requirements are not met (7 USC 2015(o)).

### *Application Process*

The application process includes completing and filing an application form, being interviewed, and having certain information verified. In addition to using information supplied by the recipients, welfare agencies use data from other agencies, such as the Social Security Administration, the Internal Revenue Service, and the State employment security agency, to verify the household's identity and income.

### **Benefits**

Benefit amounts vary with household size and income. As required by law, allotments for various household sizes are revised October 1 of each year to reflect the cost of the Thrifty Food Plan, a model plan for a low-cost nutritious diet that is developed and costed by USDA.

The benefits each household receives are redeemed for food in participating retail stores. States issue benefits in the form of debit cards, which recipients can use to purchase food. This is known as electronic benefits transfer (EBT). Welfare reform legislation required all States to use EBT by 2002, and all States have achieved full compliance.

### **Benefit Redemption**

Generally, households must use program benefits for foods to be prepared and consumed at home. There are, however, some exceptions to this general policy. For example, there are provisions for the homeless to use program benefits in authorized restaurants and for residents of some small institutional settings to participate in the program. Retailers in States where coupons are still used redeem them through the banking system without the direct involvement of State governments. However, the use of EBT increases State involvement in the redemption process. The State's EBT contractor is responsible for settlement, or payment, to retailers that have accepted EBT cards for food purchases. The contractor's "concentrator bank" makes the payment through the National Automated Clearing House (ACH) system. The concentrator bank is reimbursed for the payments by a draw made on the State's EBT benefit account with the U.S. Treasury. States usually authorize their EBT contractors to make these draws, although some States draw the cash and pay the concentrator banks themselves. The State is responsible for reconciling the payments made to retailers by its EBT contractor with the amounts drawn from its EBT account with the U.S. Treasury.

States must obtain an examination by an independent auditor of the State EBT service provider (service organization) regarding the issuance, redemption, and settlement of benefits under the Food Stamp Program in accordance with the American Institute of Certified Public Accountants (AICPA) Statement on Auditing Standards (SAS) No. 70, Service Organizations. Appendix VIII to this Supplement provides additional guidance on these examinations.

In performing audits under OMB Circular A-133 of the Food Stamp Program, an auditor may use these SAS 70 reports to gain an understanding of internal controls and obtain evidence about the operating effectiveness of controls.

### **State Responsibilities**

A State administering the Food Stamp Program must sign a Federal/State Agreement that commits it to observe applicable laws and regulations in carrying out the program (7 CFR section 272.2). Although welfare reform and subsequent legislation provided additional administrative flexibility, the Food Stamp Act remains highly prescriptive. Both the law and regulations prescribe detailed requirements for: (1) meeting program goals, such as providing timely service and rights to appeal; and (2) ensuring program integrity, such as verifying eligibility, safeguarding coupon inventories, establishing and collecting claims for benefit overpayments, and prosecuting fraud.

To ensure that States operate in compliance with the law, program regulations, and their own Plans of Operation, each State is required to have a system for monitoring and improving its administration of the Food Stamp Program (7 CFR section 275.1(a)), particularly the accuracy of eligibility and benefit determinations. This performance monitoring system includes management reviews, reviews of quality control systems, and reporting to FNS on program performance. State agencies shall conduct a review once every year for large project areas, once every two years for medium project areas, and once every three years for small project areas, unless an alternative schedule is approved by FNS. Projects are classified as large, medium, or small based on State determinations. The State must also ensure corrective action in response to the detection of program deficiencies (7 CFR sections 275.2, 275.5, and 275.16-19).

### **Federal Oversight and Compliance Mechanisms**

FNS oversees State operations through an organization consisting of headquarters and seven regional offices. In addition, about 60 field offices are often involved in State agency oversight.

FNS program oversight includes budget review and approval, reviews of financial and program reports and State management review reports, and on-site FNS reviews. Each year FNS headquarters conveys to its regions the concerns that were elevated to the national level through audits or other mechanisms. Regions combine this with their knowledge of individual States to inform the States of possible vulnerabilities to include in their internal management reviews and corrective action plans.

Although FNS uses technical assistance extensively to promote improvements in State operation of the program, enforcement mechanisms are also available. In addition to the financial rewards and penalties related to payment accuracy, FNS has other mechanisms to recover other losses and the cost of negligence (7 CFR sections 276.2 and 276.3). For other forms of noncompliance, FNS has the authority to give notice and, if improvements do not occur, withhold administrative funds for failure to implement program requirements (7 CFR section 276.4).

## **Certification Quality Control System**

The Food Stamp Program maintains an extensive quality control system required by law and regulation (7 CFR sections 275.10-14). The system provides State and national measures of the accuracy of eligibility and benefit amount determination (often referred to as payment accuracy), both underpayment and overpayment, and of the correctness of decisions to deny, terminate, or (beginning in fiscal year 2001) suspend benefits.

### *Measurement*

States are required to select a statistically valid sample of cases and to review the cases for eligibility and benefit amount. Review methods in this sample are generally more intensive than those used in determining eligibility. States submit findings of all sampled cases, including incomplete and not-subject-to-review cases, to an automated database maintained by the Federal Government. State quality control data allow a State to be aware on an ongoing basis of its level of accuracy, and allow for the identification of trends and appropriate corrective action.

The applicable FNS regional office reviews each State's sampling plan annually and re-reviews a subsample of the State quality control reviews. The FNS re-review process provides feedback to each State on its quality control system. FNS uses the State's sample and the FNS subsample in a regression formula (described in regulation) to determine payment error rates. By law, the error rate is the combined value of overpayments and under payments to participating households. FNS headquarters also reviews its regional operations and provides technical assistance to assure consistency in the national quality control system.

### *Corrective Action and Penalties*

There is a specific legislative requirement for corrective action by any State with an error rate above 6 percent (7 USC 2025 (c)(1)(B)). FNS maintains an extensive system of technical assistance for States as they develop and implement corrective action. FNS also monitors the implementation of corrective action plans. States with persistently high error rates are assessed fiscal liabilities based on the amount of benefits issued in error.

### *Implications of Quality Control for the Compliance Supplement*

The Food Stamp Program Quality Control system uses an intensive State review of a sample of active cases across the United States to measure the accuracy of Food Stamp Program eligibility determinations and benefit amounts. An FNS re-review of a subset of those cases follows. These samples are statistically valid at the State and national level. Information from Federal program oversight indicates that this sampling system is operating adequately to provide assurances that FNS is measuring the accuracy of eligibility decisions and that these data provide a basis for corrective action to improve the accuracy of eligibility decisions. Therefore, the Quality Control System sufficiently tests individual eligibility in the Food Stamp Program.

However, in those situations where computer systems are integral to the operation of the program, e.g., automated eligibility determination, the auditor should perform tests as deemed necessary to obtain assurance of the integrity of these systems. In those instances where multiple

programs share the same systems, e.g., automated intake systems for Temporary Assistance for Needy Families (TANF), Food Stamps, Medicaid, etc., testing may be done as part of the work on multiple programs.

### **Source of Governing Requirements**

The Food Stamp Program is authorized by the Food Stamp Act of 1977, as amended (7 USC 2011 *et seq.*). This description of Food Stamp Program procedures incorporates provisions of the following amendments to the Act: the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (Welfare Reform, Pub. L. 104-193, August 22, 1996), the Balanced Budget Act of 1997 (Pub. L. 105-33, August 5, 1997); and the Agricultural Research, Extension, and Reform Act of 1998 (Pub. L. 105-185, June 23, 1998); and the Farm Security and Rural Investment Act of 2002 (Pub. L. 107-171, 116 Stat. 134 *et seq.*, May 13, 2002). Food Stamp Program regulations are found in 7 CFR parts 271 through 285.

### **Availability of Other Program Information**

Additional program information is available from FNS's Food Stamp site on the Internet at <http://www.fns.usda.gov/fsp>.

## **III. COMPLIANCE REQUIREMENTS**

**In developing the audit procedures to test compliance with the requirements for a Federal program, the auditor should first look to Part 2, Matrix of Compliance Requirements, to identify which of the 14 types of compliance requirements described in Part 3 are applicable and then look to Parts 3 and 4 for the details of the requirements.**

Note: Generally, E. Eligibility, G.1 Matching, I. Procurement, and N. Special Tests and Provisions only apply to State governments. However, when States have delegated to the local governments functions normally performed by the State as administering agency, e.g., eligibility determination, issuance of food stamps, etc., the related compliance requirements will apply to the local government.

### **A. Activities Allowed or Unallowed**

Funds made available for administrative costs must be used to screen and certify applicants for program benefits, issue benefits to eligible households, conduct fraud investigations and prosecutions, provide fair hearings to households for which benefits have been denied or terminated, conduct nutrition education activities, prepare financial and special reports, operate automated data processing (ADP) systems, monitor subrecipients (where applicable), and otherwise administer the program. Portions of the award made available for specific purposes, such as ADP systems development or Employment and Training activities, must be used for such purposes (7 CFR part 277).

**E. Eligibility****1. Eligibility for Individuals**

The auditor is not required to test eligibility because detail testing of the individual case files is performed by the quality control unit and reviewed by FNS and the automated system supporting eligibility determinations and processing and tracking food stamp issuances is tested under III.N.1, "Special Tests and Provision - ADP System for Food Stamps."

**2. Eligibility for Group of Individuals or Area of Service Delivery - Not Applicable****3. Eligibility for Subrecipients - Not Applicable****G. Matching, Level of Effort, Earmarking****1. Matching**

The State is required to pay 50 percent of the costs of administering the program. Exceptions to the 50 percent reimbursement rates are: (a) 100 percent grants to administer the Employment and Training Program, and (b) an increased reimbursement rate for States with high benefit payment accuracy rates (about eight States receive this money) (7 CFR section 277.4(b)).

For Federal fiscal years 1999 through 2007, the Federal reimbursement will be decreased and the State share of administrative costs will increase by an amount equal to certain common certification costs grandfathered into the States' TANF grant levels but attributable to the Food Stamp Program (7 USC 2025(k), Section 4122 of Pub. L. 107-171, 116 Stat. 324, May 13, 2002). The amount of each State's downward adjustment was determined by the Department of Health and Human Services, and the States were notified by letter.

Costs of payment error rate reduction activities conducted under reinvestment agreements with FNS are not eligible for any level of Federal reimbursement. Private in-kind contributions are not allowable to count toward the State's share of the program's administrative cost (7 CFR sections 275.4(c) and 275.23(e)(11)(i)(C)).

**2. Level of Effort - Not Applicable****3. Earmarking - Not Applicable****I. Procurement and Suspension and Debarment**

1. *ADP Systems Development* - For competitive acquisitions of ADP equipment and services costing \$5 million or more (combined Federal and State shares), the State must submit an Advanced Planning Document (APD) for the costs to be approved

and allowable as charges to FNS. This threshold is for the total project cost. In addition, noncompetitive acquisitions of \$1 million or more require an APD. Contracts resulting from noncompetitive procurements of more than \$1 million and contracts for EBT systems, regardless of cost, also must be provided to FNS for review (7 CFR section 277.18).

2. *Procurement* - Regardless of whether the State elects to follow State or Federal rules in accordance with the A-102 Common Rule, the following requirements must be followed for procurements initiated on or after October 1, 2000:
  - a. A State or local government shall not award a contract to a firm it used to orchestrate the procurement leading to that contract. Examples of services that would disqualify a firm from receiving the contract include preparing the specifications, drafting the solicitation, formulating contract terms and conditions, etc. (7 CFR section 3016.60(b)).
  - b. A State or local government shall not apply in-State or local geographical preference, whether statutorily or administratively prescribed, in awarding contracts (7 CFR section 3016.60(c)).

## **L. Reporting**

### **1. Financial Reporting**

- a. SF-269, *Financial Status Report* - Applicable
- b. SF-270, *Request for Advance or Reimbursement* - Not Applicable
- c. SF-271, *Outlay Report and Request for Reimbursement for Construction Programs* - Not Applicable
- d. SF-272, *Federal Cash Transactions Report* - Not Applicable

### **2. Performance Reporting** - Not Applicable

### **3. Special Reporting**

Note: The requirement for State agencies to automate their food stamp programs includes automation of reporting requirements (7 CFR section 272.10(b)(2)(vi)). The testing to ensure accuracy and completeness of the following reports should be coordinated with the testing of the ADP System for Food Stamps (see III.N.1 - "Special Tests and Provisions - ADP Systems for Food Stamps").

- a. FNS-46 - *Food Stamp Program Issuance Reconciliation Report (OMB No. 0584-0080)*. This monthly report is used to account for benefits issued during a report month for each issuance reconciliation point. The FNS-46 reports the reconciliation of food stamp benefits actually issued with the State's (or county's in county-run operations)

Master Issuance File. The Master Issuance File contains records on all households eligible to receive benefits (such as a listing of the households and the benefits each is authorized to receive). Actual issuances may be recorded in the Record for Issuance (RFI) or alternative filing system. The RFI is created from the Master Issuance File and shows the amount of benefits the household is eligible to receive and the actual amount issued. Generally, one FNS-46 covers the entire State. However, if a State concurrently operates more than one type of issuance system (Authorization to Participate (ATP), mail issuance, EBT, or cash-out), its FNS-46 report(s) must separately identify the amount of benefits issued under each system.

*Key Line Items* - The following line items contain critical information:

- (1) Line 6 - *Total Issuance this month*
- (2) Line 7 - *Returns during current month*
- (3) Line 9 - *Value of authorized replacements(s) transacted*

- b. FNS-209 - *Status of Claims Against Households (OMB No. 0584-0069)*. If a household receives more food stamp benefits than it is entitled to receive, the State must establish a claim against that household and demand repayment (7 CFR section 273.18 (a)). The State is required to create and maintain a system of records for monitoring these claims against households. These State systems generate the data entered on the FNS-209 report. The minimum requirements for such systems are listed at 7 CFR section 273.18(m). The State is permitted to retain a portion of the collected repayments: 35 percent of the recovered funds from claims involving fraud or other intentional program violations; 35 percent of the funds recovered from claims generated by inadvertent household errors, collected by reducing a person's unemployment compensation benefits; and 20 percent of the recovered funds from inadvertent household error claims collected by other means. No portion of funds recovered from agency-error overpayments may be retained (7 CFR section 273.18(k)).

*Key Line Items* - The following line items contain critical information:

- (1) Line 3a *Beginning Balance* and line 13 *Ending Balance* - represent the beginning and ending balances, respectively, of the claims. Columns A, B, and C represent the number and amount of claims by claim type (i.e., intentional program violation, inadvertent household error, and State agency administrative error). The aggregate value of claims activity from the subunits should equal the State totals. The beginning and ending balances should represent the total of individual claims that comprise these balances.

- (2) Line 14 *Cash, Check, and M.O.* - represents total claims payments made in the form of cash, checks, or money orders.
  - (3) Line 15 *Food Stamps* - represents all payments in the form of food stamp coupons and EBT benefit returns.
  - (4) Line 16 *Recoupment* - represents the value of collections made through allotment reductions.
  - (5) Line 17 *Offset* - represents the total value of collections made by offsetting restored benefits against outstanding claim balances.
  - (6) Line 18b *Cash Adj.(+ or -)* - represents amendments or corrections to the collection summary of a previous report.
  - (7) Line 18c *Non-Cash Adj. (+ or -)* - represents amendments or corrections to the collection summary of a previous report relative to the return of food stamps, recoupment, or offsetting transactions.
  - (8) Line 19 *Transfers (+ or -)* - represents the claims that were contained in the collection summary of a previous report and which are being transferred from one claim category to another claim category.
  - (9) Line 20a *Cash Refunds* - represents the value of cash refunds provided to households that overpaid claims.
  - (10) Line 20b *Non-Cash Refunds* - represents the value of non-cash refunds provided to households that overpaid claims.
  - (11) Lines 21 *Total*, and 28 *Total Letter of Credit Adjustments* - represent the Total Collection Summary and the Total Letter of Credit Adjustments. The aggregate value of claims collection activity from the subunits should equal the State totals.
- c. FNS-250 - *Food Coupon Accountability Report (OMB No. 0584-0009)*. Monthly, State Agencies must submit an FNS-250 to FNS reporting monthly food stamp coupon issuance and inventory by an individual or consolidated site. The FNS-250, or equivalent information, is provided by each coupon issuer and bulk storage point that distributes food stamps. The reports are to be submitted within 45 calendar days after the last day of coupon issuance each month, and should reach the FNS by the 15th day of the second month following the last day of coupon issuance for the month (7 CFR section 274.4(b)(1)). Verification of FNS-250 information will likely require test work at individual coupon issuers or bulk storage points.

*Key Line Items* - The following line items contain critical information:

- (1) Line 14 *Total Available* - represents the total number of food coupons that were available for the month. (Testing this line will require verifying lines 8-13.)
- (2) Line 15 *Ending Inventory* - represents the total number of food coupons that were on hand at the end of the month.
- (3) Line 16 *Inventory Difference* - represents the monthly issuance activity for coupon issuers and an unauthorized shortage in inventory for bulk storage locations.
- (4) Line 19 *Total Value of Coupon Books Issued* - represents the total value of coupons issued during the month based on the physical inventory.
- (5) Line 22 *Total Value of Coupons Issued Based on Documents* - represents the total value of coupons issued according to records.

## N. Special Tests and Provisions

### 1. ADP System for Food Stamps

Note: See III.E.1, "Eligibility - Eligibility for Individuals," for the reason why the testing of the ADP system for food stamps is under this special test and provision instead of under Eligibility.

**Compliance Requirement** - State agencies are required to automate their Food Stamp Program operations and computerize their systems for obtaining, maintaining, utilizing, and transmitting information concerning the Food Stamp Program (7 CFR sections 272.10 and 277.18). This includes: (1) processing and storing all case file information necessary for eligibility determination and benefit calculation, identifying specific elements that affect eligibility, and notifying the certification unit of cases requiring notices of case disposition, adverse action and mass change, and expiration; (2) providing an automatic cutoff of participation for households which have not been recertified at the end of their certification period by reapplying and being determined eligible for a new period (7 CFR sections 272.10(b)(1)(iii) and 273.10(f) and (g)); and (3) generating data necessary to meet Federal issuance and reconciliation reporting requirements.

**Audit Objective** - Determine whether the State administering agency's ADP system for food stamps is meeting the requirements to: (1) accurately and completely process and store all case file information for eligibility determination and benefit calculation; (2) automatically cut off households at the end of their certification period unless recertified; and, (3) provide data necessary to meet Federal issuance and reconciliation reporting requirements.

## Suggested Audit Procedures

Because of the diversity of ADP hardware and software systems, it is not practical for the Compliance Supplement to provide suggested audit procedures to address each system. See Part 3, E.1.a (suggested audit procedures for eligibility for individuals relating to automated systems) in this Supplement for other guidance concerning testing ADP systems. The auditor should test the ADP system to ascertain if the system:

- a. Accurately and completely processes and stores all case file information for eligibility determination and benefit calculation.
- b. Automatically cuts off households from food stamps at the end of their certification period unless the household is recertified.
- c. Provides data necessary to meet Federal issuance and reconciliation reporting requirements. Note: This testing should be coordinated with the testing of Special Reporting (see III.L.3).

## 2. EBT Reconciliation

**Compliance Requirement** - States that use EBT must have systems in place to reconcile all of the funds entering into, exiting from, and remaining in the system each day with the State's benefit account with Treasury and EBT contractor records. This includes a reconciliation of the State's issuance files of postings to recipient accounts with the EBT contractor. States (generally through the EBT contractor that operates the EBT system) must also have systems in place to reconcile retailer credit activity as reported into the banking system to client transactions maintained by the processor and to the funds drawn down from the EBT benefit account with Treasury. States' EBT system processors should maintain audit trails that document the cycle of client transactions from posting to point-of-sale transactions at retailers through settlement of retailer credits. The financial and management data that comes from the EBT processor is reconciled by the State to the Food Stamp Program issuance files and settlement data to ensure that benefits are authorized by the State and funds have been properly drawn down. States may only draw Federal funds for authorized transactions, i.e., on-line purchases supported by entry of a valid personal identification number (PIN) or purchases using manual vouchers with telephone verification supported by a client signature and an EBT contractor authorization number (7 CFR sections 274.12(a), 274.12(g)(1) and 274.12(j)(1)).

**Audit Objective** - Determine whether the State reconciles retailer activity to client transactions, to its issuance files of postings to recipient accounts with the EBT contractor, and to postings to and drawdown activity from the State's benefit account with Treasury.

## Suggested Audit Procedures

- a. Verify that the State has a system in place to reconcile total funds entering into, exiting from, and remaining in the system each day.

- b. Select and test a sample of reconciliation(s) to verify that discrepancies are followed up and resolved. This is generally a contractor duty.
- c. Verify that the State or its contractor has a system in place to reconcile retailer credits against the information entered into the Automated Clearinghouse network and to the amount of funds drawn down by the State or the State's fiscal agent (the EBT contractor).
- d. Ascertain if the State or its contractor has recorded any non-Federal liabilities in the daily EBT reconciliation, i.e., transactions which cannot be charged to the program. If so, verify that the non-Federal liabilities were funded by non-Federal sources (i.e., the State or the contractor).

### 3. Issuance Document Security

**Compliance Requirement** - The State is required to maintain adequate security over, and documentation/records for, Authorization to Participate (ATP) cards, other documents authorizing issuance, EBT cards (7 CFR section 274.12(h)(3)), and the food stamp coupons themselves to prevent: coupon theft, embezzlement, loss, damage, destruction; unauthorized transfer, negotiation, or use of coupons; and alteration or counterfeiting of coupons and other documents authorizing issuance (7 CFR sections 274.7(b) and 274.11(c)).

**Audit Objective** - Determine whether the State maintains security over instruments used to authorize issuance of food stamp benefits.

#### Suggested Audit Procedures

- a. Observe the physical security over food stamps, ATP cards, EBT cards, and/or other negotiable instruments used in the issuance process.
- b. Verify that food stamp coupons, ATP cards, and EBT cards returned from the Postal Service are returned to inventory or destroyed.

### 4. Physical Inventory

**Compliance Requirement** - Each coupon issuer and bulk storage point that distributes food stamps is required to prepare a Food Coupon Accountability Report (FNS-250) to report monthly coupon issuance and inventory (7 CFR section 274.4(b)). Each State agency must assure that day-to-day operations of all coupon issuers comply with regulations by performing a triennial on-site review, including physical inventory, of each coupon issuer and bulk storage site under its direction (7 CFR section 274.1(c)).

**Audit Objective** - Determine whether the State agency has conducted required triennial on-site reviews, including physical inventories, at coupon issuers and bulk storage points.

## **Suggested Audit Procedures**

Determine by inquiry or inspection of records that the State agency conducts the required triennial reviews of coupon issuers and bulk storage points to ensure physical inventories are appropriate, inventories are made as required, and differences between recorded and actual inventories are reconciled.

### **5. Food Coupon Inventory Levels**

**Compliance Requirement** - State agencies must monitor the coupon inventories of coupon issuers and bulk storage points to ensure that inventories are neither excessive nor insufficient to meet the issuance needs and requirements. Inventory levels are not to exceed a "six-month supply," taking into account coupons on hand and on order (7 CFR section 274.7(a)(1)). State agencies must review the FNS-250 and other reports including shipping and transfers, returned and/or replaced mail-issuances, improperly manufactured or mutilated coupons, and reports of shortage or overage of food coupon books to ensure the accuracy of monthly inventories, compliance with required inventory levels, and accuracy and reasonableness of coupon orders.

**Audit Objective** - Determine whether food stamp coupon levels are neither excessive nor insufficient to meet the issuer's requirements.

## **Suggested Audit Procedures**

Verify that the State agencies determine that inventory levels at coupon issuers and bulk storage points are neither excessive nor insufficient to meet the issuance needs and requirements, and that inventory levels do not exceed a six-month supply, taking into account coupons on hand and on order.

### **6. Quality Control Unit**

**Compliance Requirement** - The State or local government must establish a quality control unit that is independent of program operations (7 CFR section 275.2(b)).

**Audit Objective** - Determine whether the quality control unit is organizationally independent of program operations.

## **Suggested Audit Procedures**

Ascertain that the quality control unit is organizationally independent of program operations.

## UNITED STATES DEPARTMENT OF AGRICULTURE

<b>CFDA 10.553</b>	<b>SCHOOL BREAKFAST PROGRAM (SBP)</b>
<b>CFDA 10.555</b>	<b>NATIONAL SCHOOL LUNCH PROGRAM (NSLP)</b>
<b>CFDA 10.556</b>	<b>SPECIAL MILK PROGRAM FOR CHILDREN (SMP)</b>
<b>CFDA 10.559</b>	<b>SUMMER FOOD SERVICE PROGRAM FOR CHILDREN (SFSPC)</b>

### I. PROGRAM OBJECTIVES

The objectives of the child nutrition cluster programs are to: (1) assist States in administering food services that provide healthful, nutritious meals to eligible children in public and non-profit private schools, residential child care institutions, and summer recreation programs; and (2) encourage the domestic consumption of nutritious agricultural commodities.

### II. PROGRAM PROCEDURES

#### General Overview

At the Federal level, these programs are administered by the Food and Nutrition Service (FNS) of the U.S. Department of Agriculture (USDA). FNS generally administers these programs through grants to State agencies. Each State agency, in turn, enters into agreements with subrecipient organizations for local level program operation and the delivery of program benefits and services to eligible children. The types of organizations that receive subgrants under each program are described below under "Program Descriptions." In cases where a State agency is not permitted or is not available to administer the program(s), they are administered directly by FNS regional offices. The regional offices then perform the administrative functions for local program operators that are normally performed by a State agency (7 CFR sections 210.3, 215.3, 220.3, and 225.3). For purposes of this discussion, State agencies and FNS regional offices are referred to collectively as "administering agencies."

Under 7 CFR part 250 (General Regulations and Policies - Food Distribution), USDA makes donated agricultural commodities available for use in the operation of all child nutrition programs except the SMP. FNS enters into agreements with State distributing agencies for the distribution of USDA donated commodities. The State distributing agencies, in turn, enter into agreements with local program operators, which are defined collectively as "recipient agencies." A State may designate a recipient agency to perform its storage and distribution duties. A State distributing agency may engage a commercial food processor to use the commodities in the manufacture of food products, and then deliver such manufactured products to recipient agencies.

## Program Descriptions

### *Common Characteristics*

The programs in the Child Nutrition Cluster are all variants of a basic program design having the following characteristics:

- a. Local program operators provide prepared meals to children in structured settings. Four types of meal service may be authorized: breakfast, lunch, supplements (snacks), and supper. Milk service may be authorized only under the SMP. The types a particular program operator may offer are determined first by the respective program's authorizing statute and regulations, and second by the program operator's agreement with its administering agency.
- b. While all children in attendance are entitled to receive these program benefits, children whose households meet stated income eligibility criteria generally receive their meals (or milk, where applicable) free or at a reduced price. With certain exceptions, children not eligible for free or reduced price meals or free milk must pay the full prices set by the program operator for these items. A program meal must be priced as a unit.

There are two systems of charging for program meals: "pricing" and "nonpricing" programs. In a pricing program, children who do not qualify for free meals pay a separate fee for their meals. The fee may be collected at the point of service; through a separate daily, weekly, or monthly meal charge or meal ticket payment; by earmarking a portion of the child's tuition payment expressly for food service; or through an identifiable reduction from the standard tuition rate for meals provided by parents. In a nonpricing program, no separate identifiable charges are made for meals served to enrolled children. Examples of organizations that often operate nonpricing programs include juvenile detention centers, boarding schools, other residential child-care institutions, and some private schools.

- c. Federal assistance to local program operators takes the form of cash reimbursement. In addition, USDA donates food (commodities) under 7 CFR part 250 for use in preparing meals to be served under the NSLP, SBP, and SFSPC.
- d. To obtain cash and commodity assistance, a local program operator must submit monthly claims for reimbursement to its administering agency. All meals (and half-pints of milk under SMP) claimed for reimbursement must meet Federal requirements and be served to eligible children.
- e. The program operator's entitlement to reimbursement payments is generally computed by multiplying the number of meals (and/or half-pints of milk under the SMP) served by a prescribed per-unit payment rate (called a "reimbursement rate"). Different reimbursement rates are prescribed for different categories and

types of service. “Type” refers to the kind of service (breakfast, lunch, milk, etc.), while “category” refers to the beneficiary’s eligibility (free, reduced price, or paid). Under this formula, a local program operator’s entitlement to funding from its administering agency is generally a function of the categories and types of service provided. Therefore, the child nutrition cluster programs are said to be “performance funded.”

### *Characteristics of Individual Programs*

The program-specific variants of this basic program model are outlined below.

- a. *School Nutrition Programs* (NSLP and SBP) - These programs target children enrolled in schools. For program purposes, a “school” is a public or non-profit private school of high school grade or under, or a public or licensed non-profit private residential child-care institution. At the local level, a school food authority (SFA) is the entity with which the administering agency makes an agreement for the operation of the programs. A SFA is the governing body (such as a school board) legally responsible for the operation of the NSLP and/or SBP in one or more schools. A school operated by a SFA may be approved to serve breakfast and lunch. A school in which the SFA operates an after-school care program with an educational or enrichment component may also be approved to serve supplements. See also the description of the SMP below.
- b. *SFSPC* - The SFSPC is directed toward children in low-income areas when school is not in session. It is locally operated by approved sponsors, which may include public or private non-profit SFAs, public or private non-profit residential summer camps, or units of local, municipal, county or State governments or other private non-profit organizations that develop a special summer or other school vacation program providing food service similar to that available to children during the school year under the NSLP and SBP.

A feeding site under a sponsor’s oversight may be approved to serve breakfast, lunch, supplements, and/or supper. Except for children enrolled in participating summer camps, all participating children receive their meals free. Participating summer camps must identify children eligible for free or reduced price meals and may charge those not income-eligible for free meals. Sponsors are reimbursed for operating (meal service) costs at the lesser of the performance funding formula outlined above or actual costs incurred (7 CFR section 225.9(d)(7)), except in certain cases described in III. “Compliance Requirements” below. In addition, sponsors receive payment for administrative costs under a formula described at 7 CFR section 225.9(d)(8).

Although USDA donated foods are made available under the SFSPC, they are restricted to sponsors that prepare the meals to be served at their sites and those that have entered into an agreement with a SFA for the preparation of meals.

- c. SMP - The SMP provides milk to children in schools and child-care institutions that do not participate in other Federal meal service programs. However, schools operating the NSLP and/or SBP may also participate in the SMP to provide milk to children in half-day pre-kindergarten and kindergarten programs where children do not have access to the NSLP and SBP. A SFA or institution operating the SMP as a pricing program may elect to serve free milk but there is no Federal requirement that it do so. The SMP has no reduced price benefits.

## **Program Funding**

FNS furnishes funds to State agencies by letter of credit. The State agencies use the meal reimbursement funds to support program operations by SFAs, institutions, and sponsors under their oversight, and the administrative funds to fund their own administrative costs. Funding for FNS regional office-administered programs is handled through FNS's Agency Financial Management System (AFMS).

### *Funding Program Benefits*

FNS provides cash reimbursement to each State agency for each meal served under the NSLP, SBP, and SFSPC and for each half pint of milk served under the SMP. The State agency's entitlement to cash assistance for NSLP and SBP meals, NSLP supplements, and SMP milk not reimbursed at the "free" rate is determined by multiplying the number of units served within the State by a "national average payment rate" set by FNS. Cash reimbursement to a State agency under the SFSPC is the lesser of actual costs incurred (reimbursement paid to sponsors) or the product obtained by multiplying the number of meals served by maximum rates of reimbursement established by FNS.

FNS sets the national average payment rate or maximum rate of reimbursement for each type of meal service (breakfast, lunch, supplement, supper) within each program. A national average payment rate is also set for each eligibility category within the NSLP and SBP. Basic levels of cash assistance are provided for all lunches and breakfasts, respectively. This basic rate is increased by two cents for each lunch served in SFAs in which 60 percent or more of the lunches served during the second preceding school year were served free or at a reduced price. Additional assistance is provided for lunches and breakfasts served to children eligible for free or reduced price meals. A higher rate of reimbursement (not to exceed cost) is paid for each breakfast served free or at reduced price in schools determined to be in "severe need." Milk served free under the SMP is funded at the average cost of milk. Since all meals are served free under the SFSPC, all meals of the same type are funded at the same rate.

State agencies earn commodity assistance based on the number of program meals served in schools participating in the NSLP and for certain sponsors participating in the SFSPC. The State agency's level of commodity assistance is the product of the number of meals served in the preceding year multiplied by the national average payment for donated foods.

FNS adjusts the national average payment rates and maximum rates for reimbursement annually for NSLP, SBP, and SFSPC to reflect changes in the Consumer Price Index and for the SMP to reflect changes in the Producer Price Index. FNS adjusts commodity assistance rates annually to reflect changes in the Price Index for Food Used in Schools and Institutions. The current announcements of all these assistance rates can be found on the Internet at <http://www.fns.usda.gov/cnd> (7 CFR sections 210.4(b), 220.4(b), 215.1, and 225.9(d)(9)).

A State agency uses the cash assistance obtained through performance funding to reimburse participating SFAs and sponsors for eligible meals served to eligible persons. Like “national average payments” to States, reimbursement payments are also made on a per-meal (performance funding) basis. SFAs and SFSPC sponsors receive commodities to the extent they can use them for program purposes; however, certain types of products are limited by an entitlement.

#### *Funding State-Level Administrative Costs*

In addition to funding for reimbursement payments to SFAs and sponsors, State agencies receive funding from several sources for costs they incur to administer these programs.

- a. *State Administrative Expense (SAE) Funds* - These funds are granted under CFDA 10.560, which is not included in the Child Nutrition Cluster.
- b. *SFSPC State Administrative Funds* - In addition to regular SAE grants, administrative funds are made available to State agencies under CFDA 10.559 to assist with administrative costs of the SFSPC (7 CFR section 225.5). The State agency must describe its intended use of the funds in a Program Management and Administrative Plan submitted to FNS for approval (7 CFR section 225.4).

#### **Source of Governing Requirements**

The programs included in this cluster are authorized by the Richard B. Russell National School Lunch Act (NSLA) (42 USC 1751 *et seq.*) and the Child Nutrition Act of 1966 (CNA) (42 USC 1771 *et seq.*). The implementing regulations for each program are codified in parts of 7 CFR as indicated: National School Lunch Program (NSLP), part 210; School Breakfast Program (SBP), part 220; Special Milk Program for Children (SMP), part 215; and, Summer Food Service Program for Children (SFSPC), part 225. Regulations at 7 CFR part 245 address eligibility determinations for free and reduced price meals and free milk in schools. Regulations at 7 CFR part 250 give general rules for the receipt, custody, and use of USDA donated commodities provided for use in the Child Nutrition Cluster of programs.

#### **Availability of Other Program Information**

Additional program information is available from the FNS’s Child Nutrition site on the Internet at <http://www.fns.usda.gov/cnd>. Information on the distribution of USDA donated commodities for the Child Nutrition Cluster programs is available from the FNS Food Distribution web site at <http://www.fns.usda.gov/fdd/programs/schcnp/>.

### III. COMPLIANCE REQUIREMENTS

**In developing the audit procedures to test compliance with the requirements for a Federal program, the auditor should first look to Part 2, Matrix of Compliance Requirements, to identify which of the 14 types of compliance requirements described in Part 3 are applicable and then look to Parts 3 and 4 for the details of the requirements.**

#### A. Activities Allowed or Unallowed

1. *Reimbursement for Sponsor Operating Costs (SFSPC)*

Operating costs are the costs a sponsor incurs to operate a food service under the program. The administering agency reimburses the sponsor at the lesser of its operating costs or the result of the performance funding (meals-times-rates) formula. The sponsor's operating costs may include: the cost of obtaining food (including the purchase of vended meals), labor directly involved in the preparation and service of food, the cost of nonfood supplies, rental and use allowances for equipment and space, and the cost of transporting children in rural areas to feeding sites in rural areas. A sponsor may claim as operating costs the cost of meals served to adults performing necessary food service labor, but may not claim costs of acquiring land, purchasing or constructing buildings, or altering existing buildings. Interest and the value of third-party in-kind contributions are also excluded from operating costs (7 CFR sections 225.9(d)(5) and (d)(7), and section 225.15(c)). Also see the definition of "operating costs" at 7 CFR section 225.2.

2. *Reimbursement for Sponsor Administrative Costs (SFSPC)*

Sponsor reimbursement is provided for central-level general administrative overhead, including such costs as planning and organizing, site monitoring, preparation of claims and reports, and audits. Payment to sponsors for administrative costs will be the lesser of: actual net expenses incurred for administrative costs; or the number of meals by type actually served to eligible children multiplied by the administrative rates for those meals; or the administrative budget that was approved by the administering agency and included in the program agreement, along with any approved amendments to it (7 CFR sections 225.9(d)(5) and (d)(8)), and section 225.15(c)). Also see the definition of "administrative costs" at 7 CFR section 225.2.

3. *Exception for States with Simplified SFSPC Programs*

Operating and administrative cost comparisons are not required for eligible school, public, and camp sponsors in 19 States (Alaska, Arkansas, Colorado, Idaho, Indiana, Iowa, Kansas, Kentucky, Louisiana, Michigan, Mississippi, Nebraska, New Hampshire, North Dakota, Ohio, Oklahoma, Oregon, Texas, and Wyoming) and Puerto Rico from October 1, 2004 through September 30, 2009 (42 USC 1769(f)).

## **E. Eligibility**

### **1. Eligibility for Individuals**

Any child enrolled in a participating school or summer camp, or attending a SFSPC feeding site, who meets the applicable program's definition of "child" may receive meals under the applicable program. Children belonging to households meeting nationwide income eligibility requirements may receive meals at no charge or, in the case of the NSLP and SBP, at reduced price. Children in schools operating the School Nutrition Programs, or in camps operating the SFSPC, who have been determined ineligible for free or reduced price meals pay the full price, set by the SFA or sponsor, for their meals (7 CFR sections 225.1, 225.15(e) and (f), 245.1(a), and 245.3(c); definition of "subsidized lunch (paid lunch)" at 7 CFR section 210.2; and definitions of "camp," "closed enrolled site," "open site," and "restricted open site" at 7 CFR section 225.2).

#### *a. General Eligibility*

The specific groups of children eligible to receive meals under each program are identified in the respective program's regulations.

- (1) *School Nutrition Programs (NSLP and SBP)* - A "child" is defined as: (a) a student of high school grade or under (as determined by the State educational agency) enrolled in an educational unit of high school grade or under, including students who are mentally or physically handicapped (as determined by the State) and who are participating in a school program established for the mentally or physically handicapped; (b) a person who has not reached his/her twenty-first birthday and is enrolled in a public or non-profit private residential child care institution; or (c) for meal supplements served in after-school care programs operated by an eligible school, a person who is 18 years of age or under, except that children who turn 19 during the school year remain eligible for the duration of the school year (42 USC 1766a(b); definition of "child" at 7 CFR sections 210.2 and 220.2).
- (2) *SFSPC* - A "child" is defined as: (a) any person 18 years of age and under; and (b) a person over 18 years of age, who has been determined by the State educational agency or a local public educational agency to be mentally or physically handicapped, and who participates in a public or non-profit private school program established for the mentally or physically handicapped (Definition of "children" at 7 CFR section 225.2).

- (3) *SMP* - Schools operating this program use the same definition of “child” that is used in the NSLP and SBP, except for provision (3) under the definition of “child” at 7 CFR section 210.2 regarding supplements served in after-school care programs. Where the program operates in child-care institutions, as defined in 7 CFR section 215.2(e), a “child” is any enrolled person who has not reached his/her nineteenth birthday (7 CFR section 215.2(e-1)).
- b. *Eligibility for Free or Reduced Price Meals or Free Milk*
- (1) *General Rule: Annual Certification* - A child’s eligibility for free or reduced price meals under a Child Nutrition Cluster program may be established by the submission of an annual application or statement which furnishes such information as family income and family size. SFAs, institutions, and sponsors determine eligibility by comparing the data reported by the child’s household to published income eligibility guidelines. In addition to publishing income eligibility information in the *Federal Register*, FNS makes it available on the FNS web site (<http://www.fns.usda.gov/cnd/>) under “Child Nutrition Programs, Income Eligibility Guidelines.”
    - (a) *School Nutrition Programs* - Children from households with incomes at or below 130 percent of the Federal poverty level are eligible to receive meals or milk free under the School Nutrition Programs. Children from households with incomes above 130 percent but at or below 185 percent of the Federal poverty level are eligible to receive reduced price meals. Persons from households with incomes exceeding 185 percent of the poverty level pay the full price (7 CFR sections 245.2(g), 245.3, and 245.6; sections 9(b)(1) and 17(c)(4) of the NSLA, 42 USC 1758 (b)(1) and 42 USC 1766(c)(4); sections 3(a)(6) and 4(e) of the CNA (42 USC 1772(a)(6) and 1773(e))).
    - (b) *SFSPC* - While all SFSPC meals are served at no charge, the sponsors of certain types of feeding sites must make individual determinations of eligibility for free or reduced price meals in accordance with 7 CFR section 225.15(f). See III.E.3. “Eligibility - Eligibility for Subrecipients” for more information.
    - (c) *SMP* - Eligibility for free milk in SFAs electing to serve free milk is limited to children of households meeting the income eligibility criteria for free meals under the School Nutrition Programs. The SMP has no provision for reduced price benefits (Definition of “free milk” at 7 CFR

section 215.2, and 7 CFR sections 215.7(b), 245.3, and 245.6).

Annual eligibility determinations may also be based on the child's household receiving benefits under the Food Stamp Program, Food Distribution Program on Indian Reservations (FDPIR), the Head Start Program (CFDA 93.600) (42 USC 1758(b)(6)(A)), or, under most circumstances, the Temporary Assistance for Needy Families (TANF) program (CFDA 93.558) (42 USC 1758(b)). A household may furnish documentation of its participation in one of these programs; or the school, institution, or sponsor may obtain the information directly from the State or local agency that administers these programs (7 CFR section 245.6(b)).

- (2) *Exceptions* - The following are exceptions to the requirement for annual determinations of eligibility for free or reduced price meals and free milk under the Child Nutrition Cluster programs.
- (a) *Puerto Rico and the Virgin Islands* - These two State agencies have the option to provide free meals and milk to all children participating in the School Nutrition Programs, regardless of each child's economic circumstances. Instead of counting meals and milk by type, they may determine the percentage that each type comprises of the total count using statistical surveys. The survey design must be approved by FNS (7 CFR section 245.4).
- (b) *Special Assistance Certification and Reimbursement Alternatives* - Special Assistance Certification and Reimbursement Alternatives, Provisions 1, 2 and 3, are authorized by Section 11(a)(1) of the NSLA (42 USC 1759a(a)(1)). Provision 1 may be used in schools where at least 80 percent of the children enrolled are eligible for free or reduced price meals. Under Provision 1, eligibility determinations for children eligible for free meals under the School Nutrition Programs must be made once every two consecutive school years. Children who qualify for reduced price meals are certified annually (42 USC 1759a(a)(1)(B); 7 CFR section 245.9(a)).

For Provisions 2 and 3, extended cycles are allowed for eligibility determinations. Since the schools also use alternative meal counting and claiming procedures, descriptions of Provisions 2 and 3 are presented below in III.L.3, "Reporting - Special Reporting."

- (c) *SFSPC Open Sites and Restricted Open Sites* - Determinations of individual household eligibility are not required for meals served free at SFSPC “open sites,” or “restricted open sites. See III.G.3, “Eligibility - Eligibility for Subrecipients,” for more information.

**c. Reduced Price Charges for Program Meals**

The SFA sets meal prices. However, the price for a reduced price lunch, breakfast, or snack may not exceed \$0.40, \$0.30, and \$0.15, respectively (See definition of “reduced price meal” in 7 CFR section 245.2).

- 2. Eligibility for Group of Individuals or Area of Service Delivery - Not Applicable**
- 3. Eligibility for Subrecipients**

Administering agencies may disburse program funds only to those organizations that meet eligibility requirements. Under the NSLP, SBP and SMP, this means the definition of “school food authority” (SFA) as described at 7 CFR sections 210.2, 215.2, and 220.2, respectively. Eligible SFSPC organizations are described at 7 CFR section 225.2 under the definition of “sponsor.” Additional organizational eligibility requirements apply to the SFSPC, NSLP Afterschool Snacks, and the SBP at the feeding site level (see detail below).

- a. *SFSPC* - Federal regulations at 7 CFR section 225.2 define sites in four ways:
- (1) *Open Sites* - At an open site, meals are made available to all children in the area where the site is located. This area must be one in which poor economic conditions exist (one in which at least 50 percent of the children are from households that would be eligible for free or reduced price school meals under the NSLP and the SBP). Data to support a site’s eligibility may include: (a) free and reduced price eligibility data maintained by schools that serve the same area; (b) census data; or (c) other statistical data, such as information provided by departments of welfare and zoning commissions.
  - (2) *Restricted Open Sites* - A restricted open site is one that was initially open to broad community participation, but at which the sponsor has restricted attendance for reasons of safety, security, or control. A restricted open site must serve an area in which poor economic conditions exist, and its eligibility may be documented with the same kinds of data listed above for open sites.

- (3) *Closed Enrolled Sites* - A closed enrolled site makes meals available only to enrolled children, as opposed to the community at large. Its eligibility is based not on serving an area where poor economic conditions exist, but on the eligibility of enrolled children for free or reduced price school meals. At least 50 percent of them must be so eligible. The sponsor must determine their eligibility through the application process described at 7 CFR section 225.15(f).
  - (4) *Camps* - Eligible camps include residential summer camps and nonresidential day camps that offer regularly scheduled food service as part of organized programs for enrolled children. A camp need not serve an area where poor economic conditions exist. Instead, the camp's sponsor must determine each enrolled child's eligibility for free SFSPC meals through the application requirements at 7 CFR sections 225.15(e) and (f). Unlike other sponsors, the sponsor of a camp receives reimbursement only for meals served to children eligible for free or reduced price school meals (7 CFR section 225.14(d)(1)).
- b. *SBP - Severe Need Schools* - In addition to the national average payment, FNS makes additional payments for breakfasts served to children qualifying for free or reduced price meals at schools that are in severe need. The administering agency must determine whether a school is eligible for severe need reimbursement based on the following eligibility criteria: (1) the normal reimbursement rate per meal established by the Secretary of Agriculture is insufficient to cover the costs of the school's breakfast program; (2) the school is participating in or desiring to initiate a breakfast program; and (3) 40 percent or more of the lunches served to students at the school in the second preceding school year under the NSLP were served free or at a reduced price. Administering agencies must maintain on file, and have available for reviews and audits, the source of the data to be used in making individual severe need determinations. The administering agency is also responsible for establishing systems for determining breakfast costs (7 CFR section 220.9(e)).
  - c. *NSLP - Afterschool Snacks* - Reimbursement for after-school snacks is made available to those school districts which (1) operate the NSLP in one or more of their schools and (2) sponsor or operate after-school care programs with an educational or enrichment purpose. In the case of snacks served at an eligible site located in the attendance area of a school in which at least 50 percent of the enrolled children are certified eligible for free and reduced price school meals, all snacks are served free and are reimbursed at the free rate regardless of individual eligibility. Schools and sites not located in such an area may also participate, but they must count and claim supplements as free, reduced price and paid, depending on the

eligibility status of the children served, and they must maintain documentation of eligibility for children receiving free or reduced price supplements (42 USC 1766a).

## **G. Matching, Level of Effort, Earmarking**

### **1. Matching**

#### *NSLP - State Revenue Matching Requirement*

The State is required to contribute State-appropriated funds amounting to at least 30 percent of the funds it received under Section 4 of the NSLA in the school year beginning July 1, 1980, unless otherwise exempted by 7 CFR section 210.17. In the fall of each year, FNS furnishes each State with a report giving data for the State's use in determining its matching requirements. However, the State revenues derived from the operation of the NSLP and State revenues expended for salaries and administrative expenses of the NSLP at the State level are not considered in this computation. In States with per capita income lower than the national average, the 30 percent match is proportionately reduced (sections 7(a)(1) and (2) of the NSLA, and 7 CFR section 210.17(a)).

- a. *Private School Exemption* - States that are prohibited by law from disbursing State appropriated funds to non-public schools are not required to match "General Cash Assistance" (Section 4) funds expended for meals in such schools, or to disburse to such schools any of the State revenue required to meet the matching requirements. Also, the matching requirements do not apply to schools in which the program is administered by a FNS regional office (7 CFR section 210.17(b)).
- b. *Applicable State Revenues* - State revenues, appropriated or used specifically for program purposes, are eligible for meeting the matching requirement. States use a number of methods to apply funds toward the matching requirement. For example, they may: (1) disburse such funds directly to SFAs, generally on a per-meal basis; (2) pay bills that SFAs would otherwise have had to pay themselves (such as FICA payments for school food service workers); and (3) track State-appropriated funds that SFAs have indirectly applied to the program through transfers from their general funds to their school food service funds (7 CFR section 210.17(d)).

### **2. Level of Effort - Not Applicable**

### **3. Earmarking - Not Applicable**

## I. Procurement and Suspension and Debarment

1. *Procurement* - Regardless of whether the State elects to follow State or Federal rules in accordance with the A-102 Common Rule, the following requirements must be followed for procurements initiated by State agencies and SFSPC institutions on or after October 1, 2000. The effective date of these requirements for SFAs is set by their administering agencies, but cannot be later than July 1, 2001.
  - a. *Contractor Selection* - A State agency, SFA, institution, or sponsor shall not award a contract to a firm it used to orchestrate the procurement leading to that contract. Examples of services that would disqualify a firm from receiving the contract include preparing the specifications, drafting the solicitation, formulating contract terms and conditions, etc. (7 CFR sections 3016.60(b) and 3019.43).
  - b. *Geographical Preference* - A State or local government shall not apply in-State or local geographical preference, whether statutorily or administratively prescribed, in awarding contracts (7 CFR section 3016.60(c)).
2. *Suspension and Debarment* - Mandatory awards by pass-through entities to subrecipients are excluded from the suspension and debarment rules (7 CFR section 3017.110(a)(2)(i)).

## L. Reporting

### 1. Financial Reporting

- a. SF-269, *Financial Status Report* - Applicable
- b. SF-270, *Request for Advance or Reimbursement* - Not Applicable
- c. SF-271, *Outlay Report and Request for Reimbursement for Construction Programs* - Not Applicable
- d. SF-272, *Federal Cash Transactions Report* - Not Applicable
- e. FNS-13, *Annual Report of State Revenue Matching (OMB No. 0584 - 0075)* - This report is due 120 days after the end of each school year and identifies the State revenues to be counted toward meeting the State revenue matching requirement (7 CFR section 210.17(g)).

*Key Line Item* - The following line item contains critical information:

Line 5 - *State revenues to be counted toward the State Revenue Matching Requirement*

- f. *Subrecipient Financial Reporting* - A State agency may require SFAs, institutions, and sponsors under its oversight to report information the State agency needs to prepare the financial reports identified above. Such subrecipient reports should be tested during audits of the subrecipients.

**2. Performance Reporting** - Not Applicable

**3. Special Reporting**

- a. *State Agency Special Reporting*

To receive funds for the Child Nutrition Cluster programs, a State agency administering one or more of these programs compiles the data gathered on its subrecipients' claims for reimbursement into monthly reports to its FNS regional office. Such reports present the number of meals served, by category and type, by schools or sponsors under the State agency's oversight during the report period.

An initial monthly report, which may contain estimated participation figures, is due 30 days after the close of the report month. A final report containing only actual participation data is due 90 days after the close of the report month. A final closeout report is also required in accordance with the FNS closeout-schedule. Revisions to the data presented in a 90-day report must be submitted by the last day of the quarter in which they are identified. However, the State agency must immediately submit an amended report if, at any time following the submission of the 90-day report, identified changes to the data cause the State agency's level of funding to change by more than (plus or minus) 0.5 percent. The specific reports for each program are described below.

- (1) FNS-10, *Report of School Program Operations (OMB No. 0584-0002)* - This report captures meals served under the NSLP and SBP, and half-pints of milk served under the SMP (7 CFR sections 210.5(d), 210.8, 215.10, 215.11, 220.11, and 220.13).

*Key Line Items* - The following line items contain critical information:

- (a) Item 5 - *National School Lunch Program*:
- Line 5a - *Total lunches served in the NSLP*
  - Line 5b - *Lunches served in school food authorities that qualify the State for additional payment*
  - Line 5c - *Total afterschool snacks served in all approved schools and sites*

- *Line 5d - Total afterschool snacks served in area eligible schools and sites*
- (b) *Line 6 - School Breakfast Program (Include schools with severe need)*
- (c) *Line 7 - School Breakfast Program (Severe need only)*
- (d) *Line 8 - Commodity Schools (Lunches only)*
- (e) *Item 9 - Special Milk Program:*
  - *Line 9a - Schools (Include Residential Child Care Institutions)*
  - *Line 9b - Nonresidential Child Care Institutions*
  - *Line 9c - Summer Camps*
- (f) *Item 10 - No. of Meals Served in Private Schools Only:*
  - *Line 10a - National School Lunch Program*
  - *Line 10b - Afterschool snacks*
  - *Line 10c - Afterschool snacks served in area eligible schools and sites*
  - *Line 10d - School Breakfast Program (Include Severe Need)*
  - *Line 10e - Severe Need School Breakfast Program*
- (g) *Item 11 - No. of Meals Served in Residential Child Care Institutions (RCCIs) Only:*
  - *Line 11a - National School Lunch Program*
  - *Line 11b - NSLP - Snacks*
  - *Line 11c - School Breakfast Program (Include Severe Need)*
  - *Line 11d - Severe Need School Breakfast Program*

- (2) FNS-418, *Report of the Summer Food Service Program for Children (OMB No. 0584-0280)* - This report documents the number of meals served under the SFSPC by sponsors under the State agency's oversight. Unlike the FNS-10 and FNS-44 (*Report of the Child and Adult Care Food Program*), which are generally submitted year round, the FNS-418 is filed only for the months when the program is in operation (7 CFR sections 225.8(b) and 225.9(d)(5)).

*Key Line Items* - The following line items contain critical information:

Part A - Meals Served

- (a) Lines 5 through 7 - *Breakfasts*
- (b) Lines 8 through 10 - *Lunches*
- (c) Lines 11 through 13 - *Suppers*
- (d) Lines 14 through 16 - *Supplements*
- (e) Lines 17 through 19 - *Total*

b. *Subrecipient Special Reporting*

To receive reimbursement payments for meals (and milk under the SMP) served, a SFA, institution, or sponsor must submit claims for reimbursement to its administering agency (7 CFR sections 210.8(b), 225.9(d), and 225.15(c)(2)). The claiming process is as follows:

(1) *Claiming - General Process*

At a minimum, a claim must include the number of reimbursable meals/milk served by category and type during the period (generally a month) covered by the claim. All meals claimed for reimbursement must (a) be of types authorized by the SFAs, institution's, or sponsor's administering agency; (b) be served to eligible children; and (c) be supported by accurate meal counts and records indicating the number of meals served by category and type (7 CFR sections 210.7(c), 210.8(c), and 225.9(d)).

- (a) *School Nutrition Programs* - The following types of service may be authorized for schools participating in these programs: breakfast, lunch, supplement (if the school operates an after-school care program), and milk (under the SMP). A school may be approved for the SMP only if it:
  - (i) does not operate any other Federal Child Nutrition meal

service programs; or (ii) operates the NSLP and/or SBP, but makes milk available to children in half-day pre-kindergarten or kindergarten programs who do not have access to the NSLP and SBP. All claims must be supported by accurate meal counts by category and type taken at the point of service or developed through an approved alternative procedure (7 CFR sections 210.7, 210.8, 215.8, 215.10, 220.9, and 220.11).

- (b) *SFSPC* - The meals that may be claimed under the program are: breakfast, lunch, supper, and supplement. Food service sites other than camps and sites which primarily serve migrant children may claim either: one meal each day (a breakfast, a lunch, or a supplement), or two meals each day if one is a lunch or supper and the other is a breakfast or a supplement. Camps or sites which serve meals primarily to migrant children may serve three meals or two meals and one supplement. Sponsors must also report their operating and administrative costs; these are covered in III.A, "Activities Allowed or Unallowed" (7 CFR sections 225.9(d), 225.15(c), and 225.16 (b)).

(2) *Claiming - Exceptions*

As noted above in III.E.1.b, "Eligibility for Individuals - Eligibility for Free or Reduced-Price Meals or Free Milk," schools operating the School Nutrition Programs under Special Assistance Certification and Reimbursement Alternative Provisions 2 and 3 may use alternative counting and claiming procedures. Under either provision, the schools must serve meals at no charge to all children regardless of income eligibility for program benefits; and the SFA pays, from sources other than Federal funds, for the costs of serving the lunches or breakfasts that are in excess of the value of assistance received under the NSLA and CNA (42 USC 1759a(a)(1)).

- (a) *Provision 2* - Provision 2 has a four-year cycle for annual notification and certification for free and reduced price meals. In the first year, schools must take daily counts of the number of meals served by meal category (paid, free, reduced price) and establish the percentage of meals served by category each month. In the second, third and fourth school years, schools must count only the total number of reimbursable meals served each month; the monthly percentages established in the first year are then applied to the counts taken in the corresponding months of the current

year. At the end of four years, the cycle may be extended for another four years if the State determines that the economic condition of the school's enrollment has not improved. Additional four-year extensions may be approved on the same basis (USC 1759a(a)(1)(C) and (D); 7 CFR section 245.9(b)).

- (b) *Provision 3* - Provision 3 has a four-year cycle. Cash reimbursement and commodity assistance are provided at the same level as the school received in the last year free and reduced price applications were taken and daily meal counts by category and type were made, adjusted for inflation and enrollment. Schools opting for this alternative are not required to make annual free and reduced price eligibility determinations. Free and reduced price eligibility determinations and daily meal counts by income category are only required during a base year which is not included as part of the four year cycle. Provisions exist for authorizing subsequent four-year extensions if the economic condition of the school's enrollment has not improved (42 USC 1759a(a)(1)(E)).

## **M. Subrecipient Monitoring**

State agencies administering the programs included in the Child Nutrition Cluster are required to perform specific monitoring procedures in accordance with 7 CFR sections 210.18 and 210.19(a)(4) (SBP and NSLP), 7 CFR section 215.11 (SMP), and 7 CFR section 225.7 (SFSPC).

## **N. Special Tests and Provisions**

### **1. Verification of Free and Reduced Price Applications (NSLP)**

**Compliance Requirement** - By December 15th of each school year, the SFA (or State in certain cases) must verify the current free and reduced price eligibility of households selected from a sample of applications that it has approved for free and reduced price meals, unless the SFA is otherwise exempt from the verification requirement. The verification sample size is based on the total number of approved applications on file on October 31st (7 CFR section 245.6a(a)).

A State agency may, with FNS approval, assume from SFAs under its jurisdiction the responsibility for performing the verifications. If the SFA performs the verification function it must be in accordance with instructions provided by the State agency. The SFA must follow-up on children determined ineligible for free and reduced price meals and change the category of such children determined ineligible.

SFAs (or State agencies) must select the sample by:

- a. Random sampling (the lesser of three percent or 3000 of the approved applications on file, all randomly selected), or
- b. Focused sampling in which the SFA must verify a sample that is, at a minimum, the sum of:
  - (1) The lesser of one percent or 1000 of the total number of approved applications (both income and categorical) selected from households claiming income within \$100 monthly or \$1,200 annually of the income eligibility guidelines for free and reduced price meals; and
  - (2) The lesser of .5 percent or 500 of the total number of applications that were approved based on categorical eligibility, selected from applications with a Food Stamp Program, FDPIR, or TANF case number.

Sources of information for verification include written evidence, collateral contacts, and systems of records, as described in 7 CFR section 245.6a(b).

**Audit Objective** - Determine whether the SFA (or State) selected and verified the required sample of approved free and reduced price applications and made the appropriate changes to eligibility status.

#### **Suggested Audit Procedures**

- a. Obtain the current family size and income guidelines published by FNS.
- b. Through examination of documentation, ascertain that:
  - (1) The sampling and verification of free and reduced price applications were performed, as required.
  - (2) Changes were made to eligibility status based on documentation and other information obtained through the verification process.

## **2. Accountability for Commodities**

The following compliance requirements do not apply to recipient agencies (as defined at 7 CFR section 250.3), including SFAs and SFSPC institutions. Auditors making audits of recipient agencies are not required to test compliance with these requirements.

## Compliance Requirement

### a. *Maintenance of Records*

Distributing and subdistributing agencies (as defined at 7 CFR section 250.3) must maintain accurate and complete records with respect to the receipt, distribution, and inventory of donated foods including end products processed from donated foods. Failure to maintain records required by 7 CFR section 250.16 shall be considered *prima facie* evidence of improper distribution or loss of donated foods, and the agency, processor, or entity may be required to pay USDA the value of the food or replace it in kind (7 CFR sections 250.16(a)(6) and 250.15(c)).

### b. *Physical Inventory*

Distributing and subdistributing agencies shall take a physical inventory of all storage facilities. Such inventory shall be reconciled annually with the storage facility's inventory records and maintained on file by the agency that contracted with or maintained the storage facility. Corrective action shall be taken immediately on all deficiencies and inventory discrepancies and the results of the corrective action forwarded to the distributing agency (7 CFR section 250.14(e)).

**Audit Objective** - Determine whether an appropriate accounting was maintained for donated food commodities, that an annual physical inventory was taken, and the physical inventory was reconciled with inventory records.

## Suggested Audit Procedures

- a. Determine storage facility, processing, and end use locations of all donated food commodities, including end products processed from donated foods. Determine the commodity records maintained by the entity and obtain a copy of procedures for conducting the required annual physical inventory. Obtain a copy of the annual physical inventory results.
- b. Perform analytical procedures and obtain explanation and documentation for unusual or unexpected results. Consider the following:
  - (1) Compare receipts, distribution, losses and ending inventory of donated foods for the audit period to the previous period.
  - (2) Compare distribution by entity for the audit period to the previous period.
- c. Ascertain the validity of the required annual physical inventory. Consider performing the following steps, as appropriate:
  - (1) Observe the annual inventory process at selected locations and recount a sample of commodity items.

- (2) If the annual inventory process is not observed, select a sample of significant commodities on hand as of the physical inventory date and, using the commodity records, “roll forward” the balance on hand to the current balance observed.
  - (3) On a test basis, recompute physical inventory sheets and related summarizations.
  - (4) Ascertain that the annual physical inventory was reconciled to commodity records. Investigate any large adjustments between the physical inventory and the commodity records.
- d. On a sample basis, test the mathematical accuracy of the commodity records and related summarizations. From the commodity records, vouch a sample of receipts, distributions, and losses to supporting documentation. Ascertain that activity is properly recorded, including correct quantity, proper period and, if applicable, correct recipient agency.

### 3. School Food Accounts

**Compliance Requirement** - A SFA is required to account for all revenues and expenditures of its non-profit school food service in accordance with State requirements.

A SFA must operate its food services on a non-profit basis; all revenue generated by the school food service must be used to operate and improve its food services (7 CFR sections 210.14 (a), 210.14 (c), 210.19 (a)(2), 215.7(d)(1), 220.2(o-2), and 220.7(e)(1)(i)).

**Audit Objective** - Determine whether a separate accounting is made of the school food service, Federal reimbursement payments are promptly credited to the school food service account, and transfers out of the school food service account are for the benefit of the school food service.

#### Suggested Audit Procedures

- a. Review the school food service accounting records and ascertain if a separate accounting is made for the school food service.
- b. Test Federal reimbursement payments received monthly from the administering agency to ascertain if promptly credited to the food service account.
- c. Test transfers out of the school food service account and ascertain if the transfers were for the benefit of the school food service.

**IV. OTHER INFORMATION**

FNS no longer requires recipient agencies to inventory commodities separately from purchased food. However, the value of commodities used during a State or recipient agency's fiscal year is considered Federal awards expended in accordance with the OMB Circular A-133 § \_\_\_\_.105 definition of Federal financial assistance and should be valued in accordance with § \_\_\_\_.205(g). Therefore, recipient agencies must determine the value of commodities used. FNS recommends that recipient agencies use the value of commodities delivered to them during the audit period for this purpose.

## UNITED STATES DEPARTMENT OF AGRICULTURE

### CFDA 10.557 SPECIAL SUPPLEMENTAL NUTRITION PROGRAM FOR WOMEN, INFANTS, AND CHILDREN (WIC)

#### I. PROGRAM OBJECTIVES

The objective of the Special Supplemental Nutrition Program for Women, Infants and Children (WIC) is to provide supplemental nutritious foods, nutrition education, and referrals to health care for low-income persons during critical periods of growth and development. Such persons include pregnant women, breast-feeding women up to one year postpartum, non-breast-feeding women up to six months postpartum, infants (persons under one year of age), and children under age five determined to be at nutritional risk. Intervention during the prenatal period improves fetal development and reduces the incidence of low birth weight, short gestation, and anemia.

#### II. PROGRAM PROCEDURES

##### Administration

The U.S. Department of Agriculture (USDA) Food and Nutrition Service (FNS) administers the WIC Program through grants awarded to State health departments or comparable State agencies, Indian tribal governments, bands or intertribal councils, or groups recognized by the Bureau of Indian Affairs, U.S. Department of the Interior, or the Indian Health Service (IHS) of the U.S. Department of Health and Human Services (HHS). A State administering the WIC Program must sign a Federal/State Agreement that commits it to observe applicable laws and regulations in carrying out the program. The State agencies, in turn, award subgrants to local agencies to certify applicants' eligibility for WIC Program benefits and deliver such benefits to eligible persons.

##### Program Funding

The WIC Program is a grant program that is 100 percent federally funded (7 CFR sections 246.16(a), (b), and (c)). No State matching requirement exists. Funds are awarded by FNS on the basis of funding formulas prescribed in the WIC Program regulations.

FNS allocates federally appropriated funds to WIC State agencies as grants which are divided into two parts: a component for food costs and a component for Nutrition Services and Administration (NSA) costs. Resources made available to a State agency under these two components of its initial Federal WIC formula grant may be modified by the cumulative effect of the following requirements:

##### *Reallocations and Recoveries*

The WIC Program's authorizing statute and regulations require FNS to recover unspent funds and reallocate them to State agencies.

### *Conversion Authority*

A State agency that submits a plan to increase WIC participation under a cost containment strategy, as outlined under the “Cost Containment Requirements” section below, in excess of the increases projected by FNS in the NSA funds allocation formula, may shift a portion of its food grant component to its NSA component. This “conversion authority” is a function of the “excess” participation increase and is determined by FNS (See III.A.2, “Activities Allowed or Unallowed - Exceptions”).

### *Spending Options*

Federal legislation and regulations authorize a State agency to shift a portion of its Federal WIC formula grant between grant periods (Federal fiscal years) (See III.H, “Period of Availability of Federal Funds”).

### *Rebates*

A State agency may contract with a food manufacturer to receive a rebate on each unit of the manufacturer’s product purchased with Food Instruments (FIs) redeemed by program participants. Such rebates are credits against prior expenditures made during the month in which the rebate was earned for WIC food costs (See III.B, “Allowable Costs/Cost Principles”).

### *Vendor, Participant, and Local Agency Collections*

A State agency is authorized to retain Federal program funds recovered through claims action against vendors, participants, and local agencies, and to use such recoveries for program purposes. (See III.B, “Allowable Costs/Cost Principles”).

### *Program Income*

Certain miscellaneous receipts a State agency collects as the result of WIC program operations are classified as program income (See III.J, “Program Income”).

### *State Funding*

Although the Federal Financial Participation (FFP) for WIC is 100 percent, some States voluntarily appropriate funds from their own revenues to extend WIC services beyond the level that could be supported by Federal funding alone.

## **Certification**

Applicants for WIC Program benefits are screened at WIC clinic sites to determine whether they meet the eligibility criteria in the following categories: categorical, residency, income, and nutritional risk (See III.E.1, “Eligibility - Eligibility for Individuals”).

## **Benefits**

The WIC Program provides participants with specific nutritious supplemental foods, nutrition education, and health services referrals at no cost. The authorized supplemental foods are prescribed from standard food packages according to the category and nutritional need of the participant. The seven food packages available are described in detail in WIC Program regulations.

About 75 percent of the WIC Program's annual appropriation is used to provide WIC participants with monthly food package benefits. The remainder is used to provide additional services to participants and to manage the program. Additional services provided to WIC participants include nutrition education, breast-feeding promotion and support activities, and client services, such as diet and health assessments, referral services for other health care and social services, and coordination activities.

## **Food Benefit Delivery**

Supplemental foods are provided to participants in any one of the following three ways (7 CFR section 246.12(b)):

*Direct Distribution Food Delivery Systems* (used in Mississippi, the San Felipe Indian Tribal Organization in New Mexico, and in parts of Illinois, Idaho, West Virginia, and the Acoma-Canoncito-Laguna Hospital Board of New Mexico)

The State agency and/or its agent purchases supplemental foods in bulk and issues them to participants at designated distribution facilities.

*Home Food Delivery Systems* (used in Vermont and in parts of Alaska, North Dakota, Texas, and Utah)

Arrangements with home food delivery contractors provide for the delivery of supplemental foods directly to participants' homes.

*Retail Food Delivery System* (used by most State agencies)

Negotiable FIs are issued directly to individual participants, who exchange them for authorized supplemental foods at retail stores approved as vendors by the State agency. Two types of systems are used to redeem the FIs: voucher systems and check systems. In a voucher system, the vendor submits the FIs directly to the State agency for payment; in a check system, vendors deposit FIs to their bank accounts and the State reimburses them through their banks. Generally, a participant must use an FI within 30 days of the first date of use printed on the FI; and the vendor must submit the FI for payment within 90 days of that date.

Each FI issued to a participant must have a unique serial number. A State agency is required to determine the ultimate disposition of all FIs by serial number within 150 days of the first valid date for participant use. The State agency must adjust previously reported obligations for WIC food costs in order to account for actual FI redemptions and other changes in the status of FIs.

## **Cost Containment Requirements**

In an effort to use their food funding more efficiently, all WIC State agencies in the 50 States, the District of Columbia, Puerto Rico, Guam, the Virgin Islands, American Samoa, and most Indian Tribal State agencies have implemented cost containment measures. Reducing the average food cost per person enables WIC to reach more participants with a given amount of funds. The most successful strategy has been the negotiation of competitive rebate contracts between State agencies and infant formula companies. Such contracts provide for the State agency to receive rebates on infant formula used in the program. Other cost containment measures used by State agencies include competitive bidding for juice, infant cereal, and infant juice; selection of retail vendors based on competitive prices; setting maximum redemption amounts for FIs; authorizing the use of store or generic brands of supplemental foods; and using a home delivery or direct distribution food delivery system.

## **Federal Oversight and Compliance Mechanisms**

FNS oversees State operations through an organization consisting of headquarters and seven regional offices. Federal program oversight encompasses review of the nine functional areas of the program: Organization and Management; Funding and Participation; Vendor Management; Information Systems; Certification, Eligibility, and Coordination; Nutrition Services; Civil Rights; Monitoring and Audits; and Food Delivery. Each year FNS regional offices evaluate as many of these areas as possible within available resource constraints, focusing on those areas they consider most need of review.

Although FNS uses technical assistance extensively to promote improvements in State operation of the WIC Program, enforcement mechanisms are also present. The misuse of funds through State or local agency negligence or fraud may result in the assessment of a claim (7 CFR section 246.23(a)). Claims may be established for funds lost due to FI theft or embezzlements or for unreconciled FIs (7 CFR sections 246.23(a)(2) and (4)). FNS has other mechanisms to recover other losses and the cost of negligence. For other forms of noncompliance, FNS has the authority to give notice and, if improvements do not occur, withhold administrative funds for failure to implement program requirements (7 CFR section 246.19(a)(2)).

FNS has identified the following circumstances that may indicate noncompliance with WIC program requirements: (1) redeemed FIs which the issuing local agencies had reported as voided or unclaimed; (2) a large number of consecutively numbered, unreconciled FIs issued by the same local agency; (3) redeemed FIs that appear to have been validly issued but fail to match issuance records; and, (4) participants that transacted all of their FIs on the same day as they were issued.

## **Source of Governing Requirements**

The WIC Program is authorized by section 17 of the Child Nutrition Act of 1966 (42 USC 1786). Program regulations are found at 7 CFR part 246.

## Availability of Other Program Information

For additional information, contact the applicable FNS regional office. Regional office telephone and datafax numbers, and the States each regional office serves may be found on FNS's web site (<http://www.fns.usda.gov/wic>).

## III. COMPLIANCE REQUIREMENTS

**In developing the audit procedures to test compliance with the requirements for a Federal program, the auditor should first look to Part 2, Matrix of Compliance Requirements, to identify which of the 14 types of compliance requirements described in Part 3 are applicable and then look to Parts 3 and 4 for the details of the requirements.**

### A. Activities Allowed or Unallowed

#### 1. *General Rule*

- a. Funds allocated to a State agency for food must be expended to purchase supplemental foods for participants or to redeem FIs issued for that purpose. When supplemental foods are provided to participants via direct distribution, the related warehouse facilities costs shall be allowable food costs. Food funds can also be used to purchase breast pumps for participants (7 CFR section 246.14(a) and (b)).
- b. Funds allocated for NSA must be used for the costs incurred by the State or local agency to provide participants with nutrition education, breast-feeding promotion and support, and referrals to other social and medical service providers; and to conduct participant certification, caseload management, food benefit delivery, vendor management, voter registration, and program management (42 USC 1786(h)(1)(C)(ii); 7 CFR sections 246.14(c) and (d)).

#### 2. *Exceptions*

- a. Funds allocated for food costs may be converted (be applied to NSA costs): (1) as a result of a State's plan to exceed participation levels projected by the Federal funding formula; or (2) after recovery as vendor or participant collections. Conversion due to planned participation increases is allowed only if such increases are expected to result from an approved cost containment plan (7 CFR sections 246.14(e) and 246.16(f)).
- b. Funds allocated for NSA costs but not needed for such costs may be applied to food costs (7 CFR section 246.14(a)(2)).

### 3. *Distinguishing WIC from Non-WIC Services*

Under no circumstances may the WIC NSA grant component be charged for costs that are demonstrably outside the scope of the WIC Program. WIC services may include: (a) some screening (excluding laboratory tests); (b) referrals for other medical/social services, such as immunizations, prenatal (before birth) care, perinatal care (near the time of birth from the 28th week of pregnancy through 28 days following birth), and well child care and/or family planning; and (c) follow-up on participants referred for such services. However, the cost of the services performed by other health care or social service providers to which the participant has been referred shall not be charged to the WIC grant. For example, the cost to screen, refer, and follow-up on immunizations for WIC participants may be charged to the WIC grant, but, the cost to administer the shot, or to purchase the vaccine or vaccine-related equipment, may not be charged to the WIC grant.

A hematological test for anemia, such as a hemoglobin, hematocrit, or free erythrocyte protoporphyrin test, is the only laboratory test required to determine a person's eligibility for WIC (7 CFR section 246.7(e)(1)). Accordingly, the cost of hematological tests for anemia is the only laboratory cost that may be charged to a WIC grant.

## **B. Allowable Costs/Cost Principles**

### 1. *Applicable Credits*

The following items are credits against current vendor billings or prior expenditures:

- a. *Rebates* - Rebates are credits against prior expenditures for food costs, made during the month in which the rebate was earned.
- b. *Vendor Collections* - Post-payment vendor collections are funds collected through claims assessed against food vendors for errors and overcharges. Pre-payment vendor collections are improper payments prevented as a result of reviews of FIs prior to payment; they are credits against vendor billings.
- c. *Participant Collections* - These are recoveries of improperly issued food benefits as the result of a participant, guardian or caretaker intentionally making a false or misleading statement or withholding information.
- d. *Local Agency Collections* – These are funds collected as a result of claims assessed against local agencies for program funds that were misused or otherwise diverted from program purposes due to local agency negligence or fraud.

A State agency must recognize, use, and account for these items in accordance with program regulations. At its discretion, the State agency may credit vendor, participant, and local agency collections against expenditures for food and/or NSA costs. The State agency may apply vendor, participant, and local agency collections to food and/or NSA expenditures of: (1) the fiscal year in which the initial obligation was made; (2) the fiscal year in which the claim arose; (3) the fiscal year in which the collection is received; or (4) the fiscal year following the fiscal year in which the collection is received (42 USC 1786(f)(21); 7 CFR section 246.14(e)).

2. *Capital Expenditures*

- a. FNS has authorized WIC State and local agencies to charge the full acquisition cost of non-computer equipment costing less than \$25,000 per unit without obtaining prior FNS approval, and to allow local agencies under their oversight to do likewise. FNS regional offices retain the discretion to apply a lower dollar threshold to an individual State agency and to the local agencies under its oversight, provided certain requirements apply and the State agency receives written notice.
- b. *Automated Data Processing Projects*
  - (1) FNS authorizes WIC State agencies to make automated data processing (ADP) acquisitions with a total project cost of up to \$24,999 without prior FNS approval. Instead, WIC State agencies must notify the FNS Regional Office in writing of such purchases within 60 days of the expenditure or contract execution. ADP acquisitions with a total project cost of \$25,000 to \$499,999 require a written request for prior approval from the FNS Regional Office, including an explanation of the purchase(s), description of needs, and other information appropriate to the proposed acquisition (cost allocation, procurement documents, etc, as appropriate).
  - (2) WIC State agencies are required to submit an Advance Planning Document (APD) to request prior approval of automation acquisitions with a total project cost of \$500,000 or more. Prior approval from FNS is required for such costs to be allowable charges to the WIC grant.
- c. *Other Capital Assets* - Purchases of other capital assets, such as buildings, land and improvements to buildings or land that materially increase their value or useful life, costing more than \$5000 continue to require prior approval from FNS (7 CFR section 3016.22).

## C. Cash Management

The WIC program is subject to the provisions of the Cash Management Improvement Act (CMIA). However, rebates held in State accounts are exempt from the interest provisions of the CMIA (42 USC 1786(h)(8)(J); 7 CFR section 246.15(a)).

## E. Eligibility

### 1. Eligibility for Individuals

Applicants for WIC Program benefits are screened at WIC clinic sites to determine their WIC eligibility. To be certified eligible, they must meet the following eligibility criteria (7 CFR sections 246.7(c), (d), (e), (g), and (l)):

- a. *Categorical* - Eligibility is restricted to pregnant, postpartum, and breast-feeding women, infants, and children up to their fifth birthday (7 CFR sections 246.2 (definition of each category) and 246.7(c)).
- b. *Identity and Residency* - Except in limited circumstances, WIC applicants must be physically present for eligibility screenings and must provide proof of identity. An applicant must also meet the State agency's residency requirement. Except in the case of Indian State agencies, the applicant must reside in the jurisdiction of the State. Indian State agencies may require applicants to reside within their jurisdiction. All State agencies may designate service areas for any local agency, and may require that applicants reside within the service area. A State agency must establish procedures, in accordance with guidance from FNS, to prevent the same individual from receiving duplicate benefits through participation at more than one local agency. Except under limited circumstances, WIC applicants must present proof of identity and residency at certification. Documentation of these determinations may consist of descriptions of documents evidencing the applicants' identities and residency, copies of the documents themselves, and/or the applicants' written statements when no other documentation exists. Certification procedures prescribed by the State agency set conditions for relying on these different forms of documentation (42 USC 1786(f)(23); 7 CFR sections 246.7(c)(1), 246.7(i)(3) and (4), and 246.7 (l)(2)).
- c. *Income* - An applicant must meet an income standard established by the State agency or be determined to be automatically (adjunctively) income-eligible based on documentation of his/her eligibility, or certain family members' eligibility, for the following Federal programs: (1) Temporary Assistance for Needy Families (formerly Aid To Families With Dependent Children); (2) Medicaid; or (3) Food Stamps. State agencies may also determine an individual automatically income-eligible, based on documentation of his/her eligibility for certain State-administered programs. With limited exceptions, applicants who are not adjunctively or

automatically income eligible for WIC must provide documentation of family income at their initial or subsequent certification (42 USC 1786(d)(3)(D); 7 CFR sections 246.2 (definition of “family”), 246.7(c), and 246.7(d)).

*Income Guidelines* - The income standard established by the State agency may be up to 185 percent of the poverty income guidelines issued annually by HHS or State or local income guidelines used for free and reduced-price health care. However, in using health care guidelines, the income guidelines for WIC must be between 100 and 185 percent of the poverty income guidelines. Local agency income guidelines may vary as long as they are based on the guidelines used for free and reduced-price health care (7 CFR section 246.7(d)(1)). The WIC income eligibility guidelines are issued each year in the *Federal Register* and are available on FNS’s WIC web site (<http://www.fns.usda.gov/wic>).

*Income Eligibility Determination* - Except for applicants determined to be automatically income-eligible, income is based on gross income and other cash readily available to the family or economic unit. Certain Federal payments and benefits are excluded from the computation of income. In addition, the State agency may exclude housing allowances received by military services personnel residing off military installations or in privatized housing, whether on or off-base (7 CFR section 246.7(d)(2)(iv)(A)(1)). The State agency also may exclude any cost-of-living allowance provided to military personnel who are on duty outside the contiguous States of the United States (7 CFR section 246.7(d)(2)(iv)(A)(2)).

At a minimum, in-stream (away from home base) migrant farm workers and their families with expired Verification of Certification cards shall meet the State agency’s income standard provided that the income of the family is determined at least once every 12 months (7 CFR section 246.7(d)(2)(ix)).

An Indian State agency, or a State agency acting on behalf of an Indian local agency, may submit reliable data that proves to FNS that the majority of Indian households in a local agency service area have incomes at or below the State agency’s income guidelines. In such cases, FNS may authorize the State agency to permit the use of an abbreviated income screening process whereby an applicant affirms, in writing, that his/her family income is within the State agency’s prescribed guidelines (7 CFR section 246.7(d)(2)(viii)).

State agencies may instruct local agencies to consider family income over the preceding 12 months or the family's current rate of income, whichever indicator more accurately reflects the family's income status. However, applicants in which an adult member is unemployed shall have income determined based on the period of unemployment. A State or local agency may require verification of information which it determines necessary to confirm income eligibility (7CFR sections 246.7(d)(2)(i) and (v)).

- d. *Nutritional Risk* - A competent professional authority (e.g., physician, nutritionist, registered nurse, or other health professional) must determine that the applicant is at nutritional risk. While the broad guidelines for determining nutritional risk are set forth in WIC legislation and regulations, the specific allowable nutritional risk criteria are defined in WIC policy guidance, which is updated periodically. Each State agency may choose which allowable nutritional risk criteria will be used to determine eligibility. At a minimum, the certifying agency must perform and/or document measurements of each applicant's height or length and weight. In addition, a hematological test for anemia must be performed or documented at certification if the applicant has no nutritional risk factor prescribed by the State agency other than anemia. Certified applicants with qualifying nutritional risk factors other than anemia must also be tested for anemia within 90 days of the date of certification. Program regulations set several exceptions to these general rules. The determination of nutritional risk may be based on current referral data provided by a competent professional authority who is not on the WIC staff (7 CFR sections 246.2 (definitions of "competent professional authority" and "nutritional risk") and 246.7(e)).

When an applicant meets all eligibility criteria, he/she is determined by WIC clinic staff to be eligible for program benefits. Certification periods are assigned to each participant based on categorical status for women, infants, and children (7 CFR section 246.7(g)).

A WIC local agency assigns each eligible person a priority classification according to the classification system described in 7 CFR section 246.7(e)(4). A person's priority assignment reflects the severity of his/her nutritional risk. If the local agency cannot immediately place the person on the program for lack of an available caseload slot, the person is placed on a waiting list. Caseload vacancies are filled from the waiting list in priority classification order. State agencies are expected to target program outreach and caseload management efforts toward persons at greatest nutritional risk (i.e., those in the highest priority classifications).

Pregnant women are certified for the duration of their pregnancy and for up to six weeks postpartum. Breast-feeding women may be certified for six-month intervals ending with the breast-fed infant's first birthday. Infants are certified at intervals of approximately six months, except that infants under six months of age may be certified for a period extending up to the child's first birthday, provided the quality and accessibility of health care services are not diminished. Children are certified for six-month intervals ending with the month in which the child reaches the fifth birthday. Non-breast-feeding women are certified for up to six months postpartum.

2. **Eligibility for Group of Individuals or Area of Service Delivery - Not Applicable**
3. **Eligibility for Subrecipients**

A State agency may award WIC subgrants only to organizations meeting the regulatory definition of "local agency." Such organizations include public or private non-profit health agencies, human service agencies that provide health services, IHS health units, and Indian tribal groups described in the WIC program regulations (See definition of "local agency" in 7 CFR section 246.2.).

## **H. Period of Availability of Federal Funds**

1. *Spend-Forward Option* - For WIC formula grants funds awarded prior to Federal fiscal year 2004, a State agency may spend NSA funds up to an amount equal to one percent of its total WIC formula grant for NSA costs of the following Federal fiscal year. For WIC formula grant funds awarded for Federal fiscal years 2004 and after, a State agency may spend NSA funds up to an amount equal to three percent of its total WIC formula grant for NSA costs of the following Federal fiscal year. With prior approval from its FNS regional office, the State agency may also spend NSA funds in an amount that does not exceed one-half of one percent of its total WIC formula grant, for management information systems development costs during the following Federal fiscal year. Food funds may not be "spent forward" (42 USC 1786(i)(3)(A)(ii)(I); 7 CFR section 246.16(b)(3)(ii)).
2. *Backspend Option* - A State agency may:
  - a. Spend up to one percent of the food component of its grant for food costs of the Federal fiscal year preceding the fiscal year for which the grant was awarded. This backspend authority may be raised as high as three percent with prior approval from FNS.
  - b. Spend up to one percent of its NSA grant component for food and/or NSA costs of the Federal fiscal year preceding the fiscal year for which the grant was awarded (7 CFR section 246.16(b)(3)(i)).

## **J. Program Income**

The State agency may use current year program income for costs incurred in the current fiscal year and, with the approval of FNS, for costs incurred in previous or subsequent fiscal years. Currently, the following are the only funds FNS is aware of that WIC State agencies receive that are classified as program income: (1) royalties from printed publications; (2) nominal fees, not to exceed costs, for reproducing or mailing publications, videotapes, posters, etc.; (3) interest earned on rebate funds for infant formula and other foods; (4) general grants not tied directly to foods purchased, but made for inclusion of food items in a State's food package (such as certain grants from the private sector); and (5) money received by the State agency as a result of civil money penalties or fines assessed against a vendor, and any interest charged in the collection of these penalties and fines. A State agency may use program income for any combination of food and NSA costs or other costs that further the broad objectives of the program (7 CFR section 246.15(b)).

## **L. Reporting**

### **1. Financial Reporting**

- a. SF-269, *Financial Status Report* - Not Applicable
- b. SF-270, *Request for Advance or Reimbursement* - Not Applicable
- c. SF-271, *Outlay Report and Request for Reimbursement for Construction Programs* - Not Applicable
- d. SF-272, *Federal Cash Transactions Report* - Not Applicable
- e. FNS-798, *WIC Financial Management and Participation Report (OMB No. 0584-0045)* - A State agency is required to submit monthly financial and program performance (participation) data (7 CFR section 246.25(b)).

Each WIC State agency uses the FNS-798 to report projected and actual Federal food expenditures and participation for each month of the fiscal year. Participation for any given month equals the number of individuals who received supplemental foods or FIs during that month plus the number of infants who received no supplemental foods or FIs, but were breast-fed by participating women during that month.

WIC State agencies also use the FNS-798 to provide the data FNS needs to conduct the annual grant reconciliation and closeout required by 7 CFR part 3016. The FNS-798 presents the status of the report year grant and costs adjusted by the spending options (described under III.H, "Period of Availability of Federal Funds"), which allow State agencies to shift a small portion of the WIC grant funds between Federal fiscal years. The

FNS-798 closeout report is the State's official declaration of the final status of its grant and costs for the report year.

*Key Line Items* - The following line items contain critical information:

- (1) Line 1 *Adjusted Gross Obligations* - reflects the amount of money, net of all credits used to fund food outlays except rebates, that a State agency estimates it will spend for each month's food orders or FI issuances.
  - (2) Line 2 *Estimated Rebates* - reflects the amount of money that a State agency estimates it will receive for rebates.
  - (3) Line 7 *Rebates Billed* - reflects the dollar value of bills or invoices submitted by the State to food manufacturers, such as infant formula companies, for rebate payments.
  - (4) Line 12 *Net Federal Outlays and Unliquidated Obligations* - reflects the amount of payments, net of rebates billed, program income, post-payment vendor collections, participant collections, and other credits. The State's WIC program food cost ledger account should support this amount.
  - (5) Line 18 *Total Participation* - reflects the actual number of federally supported participants for elapsed months. The participation counts should be supported by FI issuance records and participant files.
  - (6) Line 26 *Net Federal Outlays and Unliquidated Obligations for NSA Costs* - reflects gross outlays and unliquidated obligations minus program income, post-payment vendor collections, participant collections, and other credits.
- f. FNS-798A, *Addendum to WIC Financial Management and Participation Report - NSA Expenditures (OMB No. 0584-0045)* - State agencies prepare the FNS-798A annually to report: (1) NSA expenditures by function for the fiscal year being closed out; (2) the method by which NSA expenditures were charged as indirect costs; and (3) the method by which the indirect cost amount was determined. FNS uses the amounts reported in nutrition education and breast-feeding promotion and support, two of the four functional categories on the FNS-798A, to determine whether the State agencies met the statutory minimum spending level for those functions.

*Key Line Items:*

- (1) The following line items and columns contain critical information for *State-level* activities:
  - (a) Line 5a *Federal Outlays* - Column (03) - *State-Level Nutrition Education* - represents total outlays and unliquidated obligations made for State-level nutrition education costs supported by Federal grant funds and program income.
  - (b) Line 5a *Federal Outlays* - Column (04) - *State-Level Breast-feeding Promotion and Support* - represents total outlays and unliquidated obligations made for State-level breast-feeding promotion and support costs supported by Federal grant funds and program income.
  - (c) Line 5b *State Outlays* - Column (03) - *State-Level Nutrition Education* - represents total outlays and unliquidated obligations made for State-level nutrition education costs supported by State-appropriated funds plus the dollar value of any in-kind contributions received from any Federal, State or local funding source.
  - (d) Line 5b *State Outlays* - Column (04) - *State-Level Breast-feeding Promotion and Support* - represents total outlays and unliquidated obligations made for State-level breast-feeding promotion and support costs supported by State-appropriated funds plus the dollar value of any in-kind contributions received from any Federal, State or local funding source.
- (2) The following line items and columns contain critical information for *local-level* activities (Outlays and unliquidated obligations made by local agencies or made by the State agency for local clinics or other units in local communities that directly provide benefits to participants).
  - (a) Line 5a *Federal Outlays* - Column (07) - *Local-Level Nutrition Education* - represents total outlays and unliquidated obligations made for local-level nutrition education costs supported by Federal grant funds and program income.

- (b) Line 5a *Federal Outlays* - Column (08) - *Local-Level Breast-feeding Promotion and Support* - represents total outlays and unliquidated obligations made for local-level breast-feeding promotion and support costs supported by Federal grant funds and program income.
- (c) Line 5b *State Outlays* - Column (07) - *Local-Level Nutrition Education* - represents total outlays and unliquidated obligations made for local-level nutrition education costs supported by State-appropriated funds plus the dollar value of any in-kind contributions received from any Federal, State or local funding source.
- (d) Line 5b *State Outlays* - Column (08) - *Local-Level Breast-feeding Promotion and Support* - represents total outlays and unliquidated obligations made for local-level breast-feeding promotion and support costs supported by State-appropriated funds plus the dollar value of any in-kind contributions received from any Federal, State or local funding source.

(Refer to 7 CFR section 246.14(c))

- g. *Subrecipient Reporting* - A State agency may require local agencies under its oversight to report financial information the State agency needs to prepare reports identified above. These reports should be tested during audits of subrecipients.

**2. Performance Reporting** - Not Applicable

**3. Special Reporting** - Not Applicable

#### **M. Subrecipient Monitoring**

State agencies must establish an ongoing management evaluation system which includes at least the monitoring of local agency operations, the review of local agency financial and participation reports, the development of corrective action plans, the monitoring of the implementation of corrective action plans, and on-site reviews. The on-site reviews of local agencies shall include evaluation of management, certification, nutrition education, civil rights compliance, accountability, financial management systems, and food delivery systems. These reviews must be conducted on each local agency at least once every two years, including on-site reviews of a minimum of 20 percent of the clinics in each local agency or one clinic, whichever is greater (7 CFR section 246.19(b)).

## **N. Special Tests and Provisions**

### **1. Food Instrument Disposition**

**Compliance Requirement** - A State agency must account for the disposition of all FIs within 150 days of the FI's first valid date for participant use. The State agency must identify all FIs as either issued or voided; and identify issued FIs as either redeemed or unredeemed. Redeemed FIs must be identified as one of the following: (1) validly issued, (2) lost or stolen, (3) expired, (4) duplicate, or (5) not matching valid enrollment and issuance records. State agencies generally do this by analyzing computer reports that provide detailed issuance and redemption information on each FI (7 CFR section 246.12(q)).

**Audit Objective** - Determine whether the State agency's FI disposition process complies with the foregoing requirement.

#### **Suggested Audit Procedures**

- a. Obtain an understanding of the State agency's process for tracking FIs. At a minimum, this includes ascertaining how the State agency:
  - (1) Identifies the ultimate disposition of every FI; and
  - (2) Follows up on redeemed FIs that cannot be matched with valid issuances (State agencies do this by contacting the issuing local agencies and by other means).
- b. Ascertain whether the State agency provides written guidance to local agencies on how to follow up on issued FIs (redeemed and unredeemed).
- c. Inspect disposition reports to ascertain that the State agency:
  - (1) Reconciled its records to issued FIs on a one-to-one basis within the 150-day time frame set by regulation;
  - (2) Followed-up on redeemed FIs that were not validly issued and validly used, in order to determine their ultimate disposition;
  - (3) Obtained explanations for identified discrepancies; and
  - (4) Adjusted its accounting records and external reports in order to reflect the results of the disposition process.
- d. Using State agency disposition reports for one or more months of the audit period, verify the State agency's non-reconciliation rate for redeemed FIs. The State agency should use the following steps in performing the non-reconciliation rate calculation:

- (1) Determine total FIs redeemed
- (2) Determine total redeemed FIs initially identified as unreconciled (listed as redeemed with no record of issuance on exception report)
- (3) Determine total redeemed FIs finally identified as unreconciled (after follow-up with local agencies/clinics)
- (4) Calculate the unreconciled rate (#3 divided by #1)
- (5) Calculate total value of FIs redeemed
- (6) Calculate total value of FIs finally identified as unreconciled

## 2. Review of Food Instruments to Enforce Price Limitations and Detect Errors

**Compliance Requirement** – A State agency operating a retail food delivery system must take the following actions to ensure that payments of WIC food funds to vendors conform to program regulations and the State agency’s vendor agreement:

- a. *FI Review Process* - The State agency must have in place a process for reviewing all, or a representative sample of, FIs submitted by vendors for redemption. The review is done on an aggregate basis rather than on a vendor basis. Because of the wide disparity in the number of FIs processed by State agencies, there are no criteria for determining what constitutes a representative sample, other than that it must be a representative sample of FIs submitted. At a minimum, this process must be able to detect:
  - (1) Redeemed monetary amounts that exceed the maximum monetary purchase amounts established by the State agency for each type of FI.
  - (2) Other errors, including purchase price missing; participant, parent/caretaker, or proxy signature missing; vendor identification missing; FIs transacted or redeemed after the specified time period; and altered purchase price.
  - (3) Questionable FIs which, while they may not clearly contain errors, nevertheless require follow-up to determine if an error has occurred.
- b. *Follow-up on Erroneous or Questionable FIs* - The State agency must follow up on FIs containing errors and other questionable FIs detected through this process within 120 days following detection. Regulations at 7 CFR sections 246.12(k)(2) through (k)(5) describe appropriate follow-up actions (7 CFR section 246.12(k)).

**Audit Objective** – To determine whether the State agency’s system for reviewing FIs detects and follows up on erroneous or questionable FIs.

### **Suggested Audit Procedures**

- a. Obtain an understanding of the State agency's process for detecting erroneous or questionable FIs.
- b. Review the State agency's reports or other documentation of the review process, showing the results for individual FIs during the audit period. Select a sample of FIs redeemed that are covered by this documentation and analyze it to identify any FIs containing errors. If the State agency does not review all FIs, then draw the sample from only those FIs the State agency did review. Compare the FIs containing errors per the State agency's documentation against the results of analyzing the sample in order to determine whether the State agency's review process detected all erroneous or questionable FIs.
- c. Determine that the State agency followed up on all FIs for which its review process detected errors or questionable items within the required 120-day timeframe.

### **3. Compliance Investigations of High-Risk Vendors**

**Compliance Requirement** - A State agency operating a retail food delivery system must conduct compliance investigations, which consist of inventory audits and/or compliance buys, on a minimum of 5 percent of the vendors authorized as of October 1 of each year. A State agency must conduct compliance investigations on its high-risk vendors up to the 5 percent minimum. High-risk vendors are identified at least once annually using criteria developed by FNS, and/or other statistically based criteria developed by the State agency and approved by FNS. If the number of high-risk vendors exceeds 5 percent of the total, then the State agency must prioritize vendors for investigative purposes based on their potential for noncompliance and/or loss. If the number of high-risk vendors falls short of 5 percent of the total, the State agency must randomly select enough additional vendors to meet the 5 percent requirement. When a compliance investigation discloses vendor violations, the State agency must take appropriate action against the vendor. Such action includes delaying payment or establishing a claim if a violation affects payment to the vendor; imposing sanctions mandated by program regulations for certain stated violations; and imposing other, less severe sanctions prescribed by the State agency's sanction schedule for lesser violations (7 CFR sections 246.2 (definitions of "compliance buy," "high-risk vendor" and "inventory audit"), 246.12(j)(4)(i) through (iii), 246.12(k)(2) through (4), and 246.12(l)(1) and (2)).

**Audit Objective** – Determine whether the State agency made required compliance investigations and took appropriate actions against vendors.

#### **Suggested Audit Procedures**

- a. Inspect the State agency's vendor files or database to identify the vendors designated as high risk, and to determine the total number of vendors for which compliance investigations were required during the audit period.

- b. Inspect records to determine whether the State agency made the required compliance investigations and established claims against vendors or took other appropriate action based on the findings.

## UNITED STATES DEPARTMENT OF AGRICULTURE

### CFDA 10.558 CHILD AND ADULT CARE FOOD PROGRAM (CACFP)

#### I. PROGRAM OBJECTIVES

The CACFP assists States, through grants-in-aid and donated foods, to initiate and maintain non-profit food service programs for eligible children and adults in nonresidential day care settings.

#### II. PROGRAM PROCEDURES

##### General Overview

The U.S. Department of Agriculture's (USDA) Food and Nutrition Service (FNS) administers the CACFP through grants-in-aid to States. The program is administered within most States by the State educational agency. In a few States, it is administered by an alternate agency, such as the State department of health or social services. At the discretion of the Governor, different agencies within a State may administer the program's child-care and adult day-care components. In Virginia, the CACFP is directly administered by the FNS Mid-Atlantic Regional Office (MARO). For purposes of this discussion, State agencies and the MARO are referred to collectively as "administering agencies."

CACFP benefits consist of nutritious meals and snacks served to eligible children and adults who are enrolled for care at participating child care centers, adult day care centers, outside-school-hours care centers, after-school at-risk programs, family and group day care homes, and shelters. These entities are discussed in more detail below. Child and adult day care centers and outside-school-hours care centers (often referred to collectively in this discussion as "centers"), as well as after-school at-risk programs and emergency shelters, may operate independently under agreements with their administering agencies, or they may participate under the auspices of sponsoring organizations. Day care homes may participate only through sponsoring organizations. An entity with which an administering agency enters into an agreement for the operation of the CACFP, be it an independent center or a sponsoring organization, is known as an "institution."

A sponsoring organization usually does not provide child-care services itself. Rather, it assumes administrative and financial responsibility for CACFP operations in centers and day-care homes under its sponsorship. In that capacity, sponsoring organizations generally pass Federal funds received from their administering agencies through to their homes and centers; in some cases, however, sponsoring organizations provide meals to their centers in lieu of cash reimbursement.

##### *Child-Care Centers*

Eligible child-care centers include public, private non-profit, and certain proprietary child care centers, Head Start programs, and other entities which are licensed or approved to provide day care services.

### *Adult-Day Care Centers*

Public, private non-profit, and proprietary adult day-care facilities which provide structured, comprehensive services to nonresidential adults who are functionally impaired, or aged 60 and older, may participate in CACFP.

### *Outside-School-Hours Care Centers*

Outside-school-hours care centers include public, private non-profit, and proprietary organizations, licensed or approved to provide nonresidential child care services to enrolled children outside of school hours.

### *After-School At-Risk Programs*

After-school at-risk programs are structured, supervised programs that: are organized primarily to provide care to at-risk children through age 18 after school hours and on weekends and holidays during the school year; provide educational or enrichment activities; and are located in low income areas. Examples of organizations that typically offer such programs include boys' and girls' clubs, and the YMCA. In areas where Federal, State or local licensing or approval is not required, operators of these after-school programs are required to comply with State or local health and safety requirements.

### *Emergency Shelters*

Public and private non-profit emergency shelters which provide residential and food services to homeless families are eligible to participate in CACFP. Eligible shelters may receive reimbursement for serving up to three meals each day to homeless children who reside there.

### *Day-Care Homes*

A family or group day-care home is a private home licensed or approved to provide day-care services. As noted above, the provider of such services must sign an agreement with a sponsoring organization to participate in CACFP; a day-care home cannot enter into an agreement directly with the administering agency.

### *Program Funding*

Federal assistance to institutions takes the form of cash reimbursement for meals served, and USDA donated commodities or cash in lieu of commodities. An institution's entitlement to cash reimbursement is generally computed by multiplying the number of meals served, by category and type, by prescribed per-unit payment rates called "reimbursement rates." "Type" refers to the kind of meal service for which the institution seeks reimbursement (breakfast, lunch, supplement, supper). For meals served in centers, "category" refers to the economic need of the child or adult to whom a meal is served; such meals are categorized as "paid," "reduced price," or "free." Meals served in day care homes are categorized by the tiering structure (tier I or II) described in III.E.1, "Eligibility - Eligibility for Individuals" below. Under this formula, an institution's entitlement to funding from its administering agency is a function of the categories

and types of services provided. An institution establishes its entitlement to reimbursement payments by submitting claims for reimbursement to its administering agency.

Independent centers, sponsors of centers, and sponsors of day care homes may be approved to claim reimbursement for up to two reimbursable meals (breakfast, lunch or supper) and one snack, or two snacks and one meal, each day. Operators of after-school at-risk programs may claim reimbursement for one snack per child per day (except that operators of such programs in the States of Delaware, Illinois, Michigan, Missouri, New York, Oregon, and Pennsylvania may also claim supper). Homeless shelters may claim up to three meals served to each residential child each day. The specific types of meals for which an institution may claim reimbursement payments are stated in its agreement with its administering agency.

Sponsoring organizations of family day care homes also receive administrative funds related to the documented costs they incur in planning, organizing, and managing CACFP. They are the only CACFP institutions that may receive such assistance. Sponsoring organizations of centers do not receive separate administrative cost reimbursement parallel to that received by sponsors of family day care homes; nevertheless, program regulations allow them to retain for their administrative costs a portion of the meal reimbursement payments generated by their centers.

In addition to cash assistance, USDA makes donated commodities or cash-in-lieu of commodities available for use by institutions in operating the CACFP (7 CFR section 226.5). FNS enters into agreements with State distributing agencies for the distribution of commodities to CACFP institutions; the distributing agencies, in turn, enter into agreements with the institutions. The distributing agency may be the CACFP administering agency or a separate State agency.

### *Documentation Requirements*

An institution operating the CACFP must have procedures in place to collect and maintain the documentation required at 7 CFR section 226.15(e). Examples of such documentation include: (1) the institution's application and supporting documents submitted to its administering agency; (2) records of enrollment of each CACFP participant; (3) records supporting the free and reduced price eligibility determinations for children and adults enrolled in centers and for providers' children in day care homes; (4) daily records indicating the number of children and adults in attendance and the number of meals served by type and category; (5) copies of receipts, invoices and other records of CACFP costs and income required by the administering agency; (6) copies of claims for reimbursement submitted to the administering agency; and (7) documentation of non-profit operation of food service.

### **Pricing of Program Meals**

Child-care, adult day-care, and outside-school-hours centers may charge a single fee to cover tuition, meals, and all other day care services; such arrangements are called nonpricing programs. Alternatively, they may operate pricing programs, in which separate fees are charged for meals. An institution must describe its pricing policy in a free and reduced price policy statement submitted to its administering agency. The vast majority of these centers operate nonpricing programs. Nevertheless, institutions must determine the eligibility of children and

adults enrolled at these centers for free or reduced price meals because such determinations affect the reimbursement rates for meals served to the participants. After-school at-risk programs, emergency shelters, and family day care homes are prohibited from charging separately for meals.

### **Federal Assistance to States**

Program funds are provided to States through letters of credit issued under the FNS Agency Financial Management System. The States, in turn, use the funds to reimburse institutions for costs of CACFP operations, as described above, and to support State administrative expenses.

#### *Funding Program Benefits*

FNS provides a cash payment (called a “national average payment”) to each State agency for each meal served under the CACFP. A State’s entitlement to national average payments is determined by substantially the same performance-based (meals-times-rates) formula used by administering agencies to compute reimbursement payments to institutions. From the State’s standpoint, all funds received via this formula are pass-through funds that the State must use for reimbursement payments to institutions under its oversight.

FNS adjusts the national average payment rates on July 1 of each year. National average payments for meals served in centers are adjusted to reflect changes in the *Food Away From Home* series of the Consumer Price Index. Adjustments in national average payments for meals served in day care homes are adjusted on the basis of changes in the *Food at Home* series of the Consumer Price Index.

The State’s level of commodity assistance or cash in lieu of commodities is based on the numbers of lunches and suppers served in centers in the preceding year, multiplied by the national average payment for donated foods. Commodity assistance rates are also adjusted every July 1 to reflect changes in the *Food Used in Schools and Institutions* series of the Consumer Price Index.

#### *Funding State-Level Administrative Costs*

FNS makes State Administrative Expense (SAE) funds available to State agencies for administrative expenses incurred in supervising and giving technical assistance to institutions participating in CACFP. SAE requirements are prescribed at 7 CFR part 235.

Additional funds are also available to States to help State agencies and institutions comply with Federal audit requirements, and to fund costs associated with performing administrative reviews of institutions after the audit requirements have been met. A State receives such assistance in an amount equal to one and one-half percent (the percentage is reduced to one percent for fiscal years 2005 through 2007) of the payments FNS made to the State for CACFP program reimbursement to institutions during the second fiscal year preceding the year for which the funds are to be made available (42 USC 1766(i)).

## Source of Governing Requirements

The CACFP is authorized at section 17 of the Richard B. Russell National School Lunch Act (NSLA) (42 USC 1766), as amended. The program regulations are codified at 7 CFR part 226. Regulations at 7 CFR part 250 provide general rules for the receipt, custody, and use of USDA donated commodities provided for use in the CACFP.

## Availability of Other Program Information

Additional program information is available from the FNS web site at <http://www.fns.usda.gov/cnd/>. Information on the distribution of USDA-donated commodities for the CACFP is available from the FNS Food Distribution web site at <http://www.fns.usda.gov/fdd/programs/schcnp/>.

## III. COMPLIANCE REQUIREMENTS

**In developing the audit procedures to test compliance with the requirements for a Federal program, the auditor should first look to Part 2, Matrix of Compliance Requirements, to identify which of the 14 types of compliance requirements described in Part 3 are applicable and then look to Parts 3 and 4 for the details of the requirements.**

### A. Activities Allowed or Unallowed

1. *Reimbursement for Operating Costs of Child and Adult Care Centers* - The administering agency determines whether centers and sponsors of centers under its oversight shall be reimbursed solely according to the meals-times-rates formula outlined in II Program Procedures, or at the lesser of meals-times-rates or actual, documented costs. Costs claimed by the institution as operating costs must be related to preparing and serving meals to children and/or adults under the CACFP (7 CFR section 226.11(c) and definition of “operating costs” in 7 CFR section 226.2).
2. *Reimbursement for Sponsoring Organizations’ Administrative Costs* - Administrative costs are costs related to planning, organizing, and managing a food service under the CACFP (7 CFR section 226.2).
  - a. *Sponsoring Organizations of Centers* - There is no provision for sponsoring organizations of centers to receive reimbursement for administrative costs. However, a sponsor may retain a portion of a center’s meal reimbursement, not to exceed 15 percent, for its own administrative expenses (42 USC 1766(f)(2)(C)). The method to determine the portion a sponsoring organization may retain is described in III.G.3, “Matching, Level of Effort, Earmarking - Earmarking.”

- b. *Sponsoring Organizations of Family Day Care Homes* - In addition to their meal reimbursement payments, sponsoring organizations of family day care homes may receive reimbursement for their administrative costs (7 CFR section 226.12). The formula a State agency must use to determine a sponsoring organization's entitlement to administrative payments is also described in III.G.3, "Matching, Level of Effort, Earmarking - Earmarking."
  3. *Use of Reimbursements* - Reimbursement payments shall be used solely for the conduct of the food service operation or to improve such food service operations, principally for the benefit of the enrolled participants (7 CFR section 226.15(e)(14)).

### **C. Cash Management**

A sponsoring organization must disburse advance and meal reimbursement payments to centers and day care homes under its sponsorship within five working days of receiving them from its administering agency (7 CFR sections 226.16(g) and (h)).

### **E. Eligibility**

#### **1. Eligibility for Individuals**

##### *a. General Eligibility*

Any individual meeting the definition of "children" or "adult participant" at 7 CFR section 226.2, and who is enrolled in a participating nonresidential institution (or, with respect to children, an emergency shelter), may receive meals under the CACFP. These definitions are:

- (1) "Children" means (a) persons 12 years of age and under; (b) children of migrant workers 15 years of age and under; (c) persons through age 18 that are enrolled in after-school at-risk programs (except that children who turn 19 during the school year remain eligible for the duration of the school year) or in emergency shelters; and (d) mentally or physically handicapped persons, as defined by the State, enrolled in an institution or a child care facility serving a majority of persons 18 years of age and under (42 USC 1766(r) and (t)(5)(A); definitions of "children" and "enrolled child" are available at 7 CFR section 226.2).
- (2) "Adult participant" means "a person enrolled in an adult day care center who is functionally impaired ... or 60 years of age or older" (Definitions of "adult participant" and "enrolled participant" are available at 7 CFR section 226.2).

b. *Eligibility for Free or Reduced Price Meals*

- (1) *Children and Adults Enrolled in Centers* - While an independent center or sponsoring organization of centers receives Federal cash reimbursement for all meals served in centers, it receives higher levels of reimbursement for meals served to children and adults who meet Income Eligibility Criteria published by FNS for meals served free or at reduced price. Participants from households with incomes at or below 130 percent of poverty are eligible for free meals; and participants with household incomes between 130 percent and 185 percent of poverty are eligible for reduced price meals. The Income Eligibility Guidelines and Reimbursement Rates are published in the *Federal Register* and on the FNS web site at <http://www.fns.usda.gov/cnd>. Institutions must determine each enrolled participant's eligibility for free and reduced price meals in order to claim reimbursement for the meals served to that individual at the correct rate (7 CFR sections 226.17(b)(7), 226.19(b)(8)(i), and 226.19a(b)(8)).

A participant's eligibility may be established by the following methods:

- (a) *General Rule: Household Application* - The participant's household may submit an income eligibility statement that provides information about household size and income. The information submitted by each household is compared with USDA's published Income Eligibility Guidelines. A household is not required to furnish documentation to support the information given in its income eligibility statement; however, that information is subject to verification under 7 CFR 226.23(h) (7 CFR sections 226.23(e)(1)(ii) and (iii), and 226.23(e)(4)).
- (b) *Exception: Categorical Eligibility* - Children and adults may be determined categorically eligible for free and reduced price meals by virtue of their participation in certain other programs. For children, such programs include the Food Stamp Program, Food Distribution Program on Indian Reservations (FDPIR), or State programs funded through Temporary Assistance for Needy Families (TANF). Categorically eligible adults include those who receive Food Stamp Program, FDPIR, Supplemental Security Income (SSI), or Medicaid benefits. Categorically eligible participants must indicate on the income eligibility statement the other program for which they are eligible. No income eligibility statement is

required for children participating in the Head Start Program or for pre-kindergarten children participating in the Even Start Programs, nor is any eligibility determination required beyond documenting their participation in Head Start or Even Start (7 CFR sections 226.23 (e)(1)(iv) and (v); 42 USC 1766(c)(6)).

- (2) *Children Enrolled in Family Day Care Homes* - A tiering structure prescribed by program statute and regulations forms the basis for meal reimbursement payments to sponsoring organizations of day care homes. A home is classified as tier I or tier II, depending on the home's location or the provider's income eligibility.

Tier I day care homes are those operated by providers whose households meet the income standards for free or reduced price meals, as outlined above; or those located in low-income areas. A low-income area is one where at least 50 percent of the children are eligible for free or reduced price school meals. Sponsoring organizations may use census block data or elementary school enrollment data to determine low-income areas (7 CFR sections 226.2 (definitions of "low-income area" and "tier I day care home") and 226.15 (e)(3) and (f)).

Tier II homes are those family day-care homes which do not meet the location or provider income criteria for a tier I home. Per-meal reimbursement rates for meals served in tier II homes are lower than corresponding rates for tier I homes. The provider in a tier II home may nevertheless elect to have the sponsoring organization identify income-eligible children, so that meals served to those children who qualify for free and reduced price meals would be reimbursed at the higher tier I rate (7 CFR section 226.23(e)(1)(i)).

Meals served to a day care home provider's own children are not reimbursable unless all of the following conditions are met: (a) such children are enrolled and participating in the CACFP during the time of the meal service; (b) enrolled, nonresidential children are present and participating in the CACFP; and (c) the provider's own children are eligible for free or reduced price meals (7 CFR section 226.18(e)).

- (3) *Children Enrolled in After-School At-Risk Programs* - Eligible after-school programs must be located in geographical areas where 50 percent or more of the children are eligible for free or reduced price meals under the School Nutrition Programs (CFDA 10.553 and 10.555), as demonstrated by the free and reduced price eligibility data maintained by the school serving the area.

Individual eligibility determinations for children attending these programs are not required (42 USC 1766(r)).

- (4) *Children Enrolled in Emergency Shelters* - Children enrolled in emergency shelters receive meals at no charge (42 USC 1766(t)(5)(C)).

**2. Eligibility for Group of Individuals or Area of Service Delivery - Not Applicable**

**3. Eligibility for Subrecipients**

- a. Administering agencies may disburse CACFP funds only to those organizations that meet the eligibility requirements stated in the following program requirements: (1) generic requirements for all institutions at 7 CFR section 226.15 and 42 USC 1766(a)(6) and (d)(1); (2) additional requirements for sponsoring organizations at 7 CFR section 226.16; (3) additional requirements for child care centers (whether independent or sponsored) at 7 CFR section 226.17; (4) additional requirements for day care homes (which must be sponsored) at 7 CFR section 226.18; (5) additional requirements for outside-school-hours centers at 7 CFR section 226.19; (6) additional requirements for adult day care centers (whether independent or sponsored) at 7 CFR section 226.19a; (7) additional requirements for after-school at-risk programs at 42 USC 1766(r); and (8) additional requirements for emergency shelters at 42 USC 1766(t).
- b. Proprietary child care and outside-school-hours centers may participate in the CACFP if they meet either of the following two criteria: (1) at least 25 percent of the enrolled children or 25 percent of the licensed capacity, whichever is less, are funded under Title XX of the Social Security Act; or (2) as of June 30, 2004, at least 25 percent of the children in their care are eligible for free or reduced price meals(42 USC 1766(a)(2)(B)).
- c. Proprietary adult day care centers may be eligible for CACFP if at least 25 percent of their participants receive benefits under Title XIX or Title XX of the Social Security Act (7 CFR section 226.2 (definitions of “proprietary Title XIX center” and “proprietary Title XX center”)).

**G. Matching, Level of Effort, Earmarking**

- 1. Matching** - Not Applicable
- 2. Level of Effort** - Not Applicable

### **3. Earmarking**

- a. *Sponsoring Organizations of Day Care Homes* - Administrative cost reimbursement to sponsoring organizations of day care homes is limited to the lesser of the following factors on a cumulative year-to-date basis: (1) the sponsoring organization's approved administrative budget; (2) actual administrative costs less income to the program; or (3) the appropriate monthly rates per home, multiplied by the number of operating homes in each month. In addition, during any fiscal year, administrative payments to a sponsoring organization may not exceed 30 percent of the total amount of administrative payments and program (meal reimbursement) payments for day care home operations (7 CFR section 226.12(a))
- b. *Sponsoring Organizations of Centers* - There is no provision for sponsoring organizations of centers to receive a separate reimbursement for administrative costs. However, sponsors may retain up to 15 percent from a center's reimbursement for its administrative expenses. State agencies may waive this limit if certain regulatory criteria are met (7 CFR sections 226.6(f)(3) and 226.16(b)(1)).

### **I. Procurement and Suspension and Debarment**

1. *Procurement* - Regardless of whether the State elects to follow State or Federal rules in accordance with the A-102 Common Rule, the following requirements must be followed for procurements initiated on or after October 1, 2000:
  - a. A State agency or institution shall not award a contract to a firm it used to orchestrate the procurement leading to that contract. Examples of services that would disqualify a firm from receiving the contract include preparing the specifications, drafting the solicitation, formulating contract terms and conditions, etc. (7 CFR sections 3016.60(b) and 3019.43).
  - b. A State or local government shall not apply in-State or local geographical preference, whether statutorily or administratively prescribed, in awarding contracts (7 CFR section 3016.60(c)).
2. *Suspension and Debarment* - Mandatory awards by pass-through entities to subrecipients are excluded from the suspension and debarment rules (7 CFR section 3017.110(a)(2)(i)).

### **L. Reporting**

#### **1. Financial Reporting**

- a. SF-269, *Financial Status Report* - Applicable
- b. SF-270, *Request for Advance or Reimbursement* - Not Applicable

- c. SF-271, *Outlay Report and Request for Reimbursement for Construction Programs* - Not Applicable
- d. SF-272, *Federal Cash Transactions Report* - Not Applicable
- e. *Subrecipient Financial Reporting* - A State agency may require subrecipients to report information the State agency needs to prepare the financial reports identified above. Such subrecipient reports should be tested during audits of the subrecipients.

**2. Performance Reporting** - Not Applicable

**3. Special Reporting**

a. *State Agency Special Reporting*

FNS-44, *Report of the Child and Adult Care Food Program (OMB No. 0584-0078)* - To receive CACFP funds, a State agency administering the program compiles the data gathered on its subrecipients' claims for reimbursement into monthly reports to its FNS regional office. Such reports present the number of meals served, by category and type, in institutions under the State agency's oversight during the report month.

An initial monthly report, which may contain estimated participation figures, is due 30 days after the close of the report month. A final report containing only actual participation data is due 90 days after the close of the report month. A final closeout report is also required, in accordance with the FNS closeout schedule. Revisions to the data presented in a 90-day report must be submitted by the last day of the quarter in which they are identified. However, the State agency must immediately submit an amended report if, at any time following the submission of the 90 day report, identified changes to the data cause the State agency's level of funding to change by more than (plus or minus) 0.5 percent.

*Key Line Items* - The following line items contain critical information:

- (1) *Part A - No. Homes*
  - (a) Line 6 - *No. of sponsoring organizations of day care homes administering between (ranges for numbers of homes given in columns)*
  - (b) Line 7 - *No. of homes for which sponsors are eligible to receive reimbursement based on rate for (ranges for numbers of homes given in columns)*

(2) *Part E*

- (a) Lines 22 through 30 - *Breakfasts*
- (b) Lines 31 through 39 - *Lunches*
- (c) Lines 40 through 48 - *Suppers*
- (d) Lines 49 through 57 - *Supplements*
- (e) Lines 58 through 60 - *Total Free, Reduced Price, and Paid Meals Served (Respectively)*

b. *Subrecipient Special Reporting*

To receive reimbursement payments for meals served, an institution must submit claims for reimbursement to its administering agency. A claim must include the number of meals served by category and type during the period (generally a month) covered by the claim. All meals claimed for reimbursement must be of types authorized by the institution's administering agency; must be served to eligible children or adults; and must be supported by accurate meal counts and records indicating the number of meals served by category and type. Reimbursement is not allowed for meals served to a participant who is not enrolled for care, meals served in excess of an institution's licensed or authorized capacity, meal types that are not approved in the institution's agreement with its administering agency, or meals served in excess of the maximum number of approved meal services (7 CFR sections 226.10(c), 226.15(g), 226.17(b)(4), 226.19(b)(5), and 226.19a(b)(6)).

- (1) *Meals Served in Child and Adult Care Centers* - Several variants are available for reporting participation under the meals-times-rates reimbursement formula. They include: (a) reporting actual meal counts by category and type; (b) applying "blended per-meal rates" to actual counts of meals served by type; and (c) applying the center's "claiming percentage" for each category to its actual count of each type of meal served. The claiming percentage for each category is the ratio of enrolled persons eligible for meals in that category to all enrolled persons. The institution's agreement with its administering agency identifies the variant to be used (7 CFR sections 226.9(b) and 226.11(b)).
- (2) *Meals Served in Family Day Care Homes* - Like a sponsor of centers, a family day care home sponsor must claim reimbursement for meals by category and type. With respect to day care homes, however, "category" refers to the tiering structure (tier I or tier II) rather than to an individual's income eligibility, as described under

III.E.1, “Eligibility - Eligibility for Individuals,” (7 CFR section 226.13(b)).

To develop the information needed to prepare a claim, the sponsoring organization requires each day care home under its sponsorship to report the number of reimbursable meals served during each claim month. The sponsoring organization collects the number of meals served, by type, from tier I homes and from tier II homes that elect not to request the sponsoring organization to make individual income eligibility determinations for enrolled children (7 CFR sections 226.13(d)(1) and (2)). If a tier II day care home provider has elected to have its sponsoring organization make individual income eligibility determinations, program regulations provide several options for reporting the number of meals eligible for reimbursement at the tier I and II rates, respectively (7 CFR section 226.13(d)(3)).

The reimbursement rates for lunches and suppers served in family day care homes whose sponsoring organizations have elected to receive USDA donated commodities are reduced by the value of the commodities (7 CFR section 226.13(c)).

- (3) *Meals Served in After-School At-Risk Programs* - Reimbursement payments for snacks served to children in after-school at-risk programs are limited to one snack per child per day. In the States of Delaware, Illinois (effective November 28, 2001), Michigan, Missouri, New York, Oregon, and Pennsylvania, however, operators may also claim one supper per child per day. Snacks and suppers served in after-school at-risk programs are provided at no charge and reimbursed at the “free” rate (42 USC 1766(r)).
- (4) *Meals Served in Emergency Shelters* - A shelter or its sponsoring organization may claim reimbursement only for three meals, or two meals and one supplement, per child per day. All such meals are provided at no charge and reimbursed at the free rate (42 USC 1766(t)(5)(B) and (C)).

An institution must report such information, in addition to meal counts, as its administering agency determines necessary to support the reimbursement claimed. For centers and sponsors of centers in States that elect to reimburse at the lesser of meals-times-rates or documented costs, such information includes their operating (meal production) costs. For sponsors of family day care homes, such information includes their administrative costs (7 CFR sections 226.7(m), 226.9(c) and (d), 226.10(c), 226.11(d), and 226.12(a)(1)). This aspect of the claiming process is discussed in III.A, “Activities Allowed or Unallowed.”

## **M. Subrecipient Monitoring**

The administering agency is responsible for monitoring the institution's non-profit status to ensure that all reimbursements shall be used solely for the conduct of the food service operation or to improve such food service operations, principally for the benefit of the enrolled participants (7 CFR section 226.7(b)) and 42 USC 1766 (d)(1)(B)).

The administering agency is required to assess institutional compliance by performing on-site reviews of independent centers, sponsoring organizations of centers, and sponsoring organizations of day care homes, including reviews of new organizations, in accordance with a schedule prescribed in 7 CFR section 226.6(m) and 42 USC 1766 (d)(2)(A).

## **N. Special Tests and Provisions**

### **1. Accountability for Commodities**

#### **Compliance Requirement**

The following compliance requirements do not apply to recipient agencies (as defined at 7 CFR section 250.3), including CACFP institutions. Auditors making audits of recipient agencies are not required to test compliance with these requirements.

#### *a. Maintenance of Records*

Distributing and subdistributing agencies (as defined at 7 CFR section 250.3) must maintain accurate and complete records with respect to the receipt, distribution, and inventory of donated foods including end products processed from donated foods. Failure to maintain records required by 7 CFR section 250.16 shall be considered prima facie evidence of improper distribution or loss of donated foods, and the agency, processor, or entity may be required to pay USDA the value of the food or replace it in kind (7 CFR sections 250.16(a)(6) and 250.15(c)).

#### *b. Physical Inventory*

Distributing and subdistributing agencies and institutions shall take a physical inventory of all storage facilities. Such inventory shall be reconciled annually with the storage facility's inventory records and maintained on file by the agency which contracted with or maintained the storage facility. Corrective action shall be taken immediately on all deficiencies and inventory discrepancies and the results of the corrective action forwarded to the distributing agency (7 CFR section 250.14(e)).

**Audit Objective** - Determine whether an appropriate accounting was maintained for donated food commodities, that an annual physical inventory was taken, and that the physical inventory was reconciled with inventory records.

### **Suggested Audit Procedures**

- a. Determine storage facility, processing, and end use locations of all donated food commodities, including end products processed from donated foods. Ascertain the commodity records maintained by the entity and obtain a copy of procedures for conducting the required annual physical inventory. Obtain a copy of the annual physical inventory results.
- b. Perform analytical procedures, obtain explanation and documentation for unusual or unexpected results. Consider the following:
  - (1) Compare receipts, distributions, losses and ending inventory of donated foods for the audit period to the previous period.
  - (2) Compare distribution by entity for the audit period to the previous period.
- c. Ascertain the validity of the required annual physical inventory. Consider performing the following steps, as appropriate:
  - (1) Observe the annual inventory process at selected locations and recount a sample of commodity items.
  - (2) If the annual inventory process is not observed, select a sample of significant commodities on hand as of the physical inventory date and, using the commodity records, “roll forward” the balance on hand to the current balance observed.
  - (3) On a test basis, recompute physical inventory sheets and related summarizations.
  - (4) Ascertain that the annual physical inventory was reconciled to commodity records. Investigate any large adjustments between the physical inventory and the commodity records.
- d. On a sample basis, test the mathematical accuracy of the commodity records and related summarizations. From the commodity records, vouch a sample of receipts, distributions, and losses to supporting documentation. Ascertain that activity is properly recorded, including correct quantity, proper period and, if applicable, correct recipient agency.

**IV. OTHER INFORMATION**

FNS no longer requires recipient agencies to inventory commodities separately from purchased food. However, the value of commodities used during a State or recipient agency's fiscal year is considered Federal awards expended in accordance with the OMB Circular A-133 § \_\_\_\_.105, definition of Federal financial assistance and should be valued in accordance with § \_\_\_\_.205(g). Therefore, recipient agencies must determine the value of commodities used. FNS recommends that recipient agencies use the value of commodities delivered to them during the audit period for this purpose.

## UNITED STATES DEPARTMENT OF AGRICULTURE

### CFDA 10.566 NUTRITION ASSISTANCE FOR PUERTO RICO

#### I. PROGRAM OBJECTIVES

The objective of the Puerto Rico Nutrition Assistance Program (NAP) is to help needy residents of the Commonwealth of Puerto Rico (PR) meet their nutritional needs.

#### II. PROGRAM PROCEDURES

##### Administration

Funds for the NAP are appropriated annually. The Food and Nutrition Service (FNS) of the USDA provides an annual block grant to the PR Department of the Family to cover the full cost of program benefits and 50 percent of the costs of administering the program. As a condition of receiving the grant, PR must submit an annual plan of operation for review and approval by FNS. FNS provides monthly increments to PR's NAP letter-of-credit authorization on the basis of budget estimates contained in the approved plan. FNS also monitors program operations to assure program integrity. These monitoring activities include reviewing financial reports and making on-site management reviews of selected program operations (7 CFR sections 285.2(a) and 285.3).

##### Benefits

Under the NAP, participating households receive nutritional benefits to supplement their incomes. They must use these program benefits to purchase foods for preparation and consumption at home. The amount of a household's monthly benefit payment depends on the household's characteristics, financial circumstances, and the funds available for distribution. PR establishes the eligibility and benefit levels for the program. The benefits are revised October 1 of each year to consider the nutritional needs of PR's needy population and to provide for the distribution of available block grant funds.

A household receives its monthly benefit payment electronically. PR issues each client household a debit card with which to access the benefits. Since September 2001, 75 percent of each household's monthly benefit has been designated for use in making food purchases at retailers authorized by PR. The remaining 25 percent is a cash benefit. Clients may use their debit cards to obtain cash at ATMs, or to combine their cash and non-cash benefits in food purchases from authorized retailers. PR monitors retailer and household compliance.

##### Benefit Redemption

NAP benefits are administered through an electronic benefit transfer (EBT) system. PR establishes a benefit account to control the issuance and use of each household's benefits. Benefit issuance takes the form of posting monthly increments to the client's account: 75 percent to the non-cash account and 25 percent to the cash account. ATM transactions generate charges against the client's cash account. Purchases at authorized retailers generate on-line charges

against the client's non-cash account; these are resolved by crediting the retailers for the amount of client purchases. PR must reconcile the funds exiting the EBT system and paid to retailers with amounts drawn from its EBT benefit account with the Government Development Bank (GDB). Cash drawn from PR's letter-of-credit is used to settle accounts with the GDB. A service provider is used to process NAP EBT transactions.

PR obtains an examination by an independent auditor of the EBT service provider (service organization) regarding the issuance, redemption, and settlement of benefits in accordance with the American Institute of Certified Public Accountants (AICPA) Statement on Auditing Standards (SAS) No. 70, Service Organizations.

### **Employment Services for NAP Participants**

Since October 1988, PR's annual plan of operation has called for using a prescribed portion of its NAP grant for program components designed to move NAP participants who are able to work into the workforce. PR initially met this need through the Special Wage Incentive Program (SWIP). Beginning in May 2005, PR began phasing out SWIP and replacing it with Training, Experience & Employment for NAP Participants (TEENAP). TEENAP is being phased in during Federal Fiscal Year 2006.

The PR Department of the Family operated SWIP through contracted sponsoring agencies, which performed job placement services for NAP participants. PR reimbursed the sponsoring agencies for 50 percent of the costs they incurred completing each job placement, and employers for 50 percent of the wages they paid employees recruited through SWIP. These employers entered into wage contracts with PR. Although PR ceased making SWIP placements on May 6, 2005, some existing contracts are expected to remain in effect through May 6, 2008 (PR Annual Plan of Operation for Fiscal Year 2005, Section D (*SWIP Attachments*)).

Under TEENAP, PR will perform in-house the functions previously performed by SWIP sponsoring agencies. Wage incentives to employers will not be used. Rather, PR will incur administrative costs as a result of providing NAP participants with the skills and job experience that will facilitate their entry into full-time, permanent employment. Examples of such activities include coaching in how to look for a job, vocational/technical training, basic education, employability skills workshops, and volunteer community service work. PR's administrative costs of conducting these activities are reimbursable from Federal NAP funds and subject to the 50 percent matching requirement (see III.G.1).

### **Source of Governing Requirements**

The NAP is authorized by section 19 of the Food Stamp Act of 1977 (7 USC 2028), amended by the Farm Security and Rural Investment Act of 2002 (Pub. L. 107-171, 116 Stat. 134 *et seq.*, May 13, 2002). USDA regulations pertaining to NAP are found in 7 CFR part 285. Many program requirements are established through PR's approved annual plan of operation.

### III. COMPLIANCE REQUIREMENTS AND SUGGESTED AUDIT PROCEDURES

**In developing the audit procedures to test compliance with the requirements for a Federal program, the auditor should first look at Part 2, Matrix of Compliance Requirements, to identify which of the 14 types of compliance requirements described in Part 3 are applicable and then look to Parts 3 and 4 for the details of the requirements.**

#### A. Activities Allowed or Unallowed

The annual plan of operation submitted by the PR Department of the Family must include a description of PR's program for providing nutrition assistance to needy persons and the eligible SWIP and TEENAP activities. The nutrition assistance PR actually provides must conform to the approved plan (7 CFR section 285.3(b)(3); PR Annual Plan of Operation).

#### E. Eligibility

##### 1. Eligibility for Individuals

- a. The PR Department of the Family is required to identify in its annual plan the population eligible for NAP benefits. In testing the propriety of eligibility determinations and disbursements for NAP benefits, the auditor shall apply the eligibility criteria established by the PR Department of the Family and identified in the annual plan (7 CFR section 285.3(b)(2)).
- b. Individuals placed in the SWIP or TEENAP must be NAP participants (PR Annual Plan of Operation for Fiscal Year 2005, Section D (*SWIP Attachments*) and PR Annual Plan of Operation for Fiscal Year 2006, Attachment 2 (Revised Amendments/Section I)).

##### 2. Eligibility for Group of Individuals or Area of Service Delivery - Not Applicable

##### 3. Eligibility for Subrecipients - Not Applicable

#### G. Matching, Level of Effort, Earmarking

##### 1. Matching

- a. The NAP grant provided by FNS is intended to cover 100 percent of PR's expenditures for NAP benefits and 50 percent of the related administrative expenses. PR must provide funds for its 50 percent share of the administrative expenses (7 CFR section 285.2(a)).
- b. Sponsoring agencies must provide 50 percent of their SWIP administrative costs (PR Annual Plan of Operation for Fiscal Year 2005, Section D (*SWIP Attachments*), Part D, Item 1).

**2. Level of Effort - Not Applicable**

**3. Earmarking - Not Applicable**

**H. Period of Availability of Federal Funds**

Payments received by PR for a fiscal year may not exceed the amount authorized for the grant or the total NAP cost eligible for funding, whichever is less, for that fiscal year. Funds for payments for any prior fiscal year expenditures must be claimed against the funding for that fiscal year; however, funds collected from claims are credited to the fiscal year in which the collection occurred (7 USC 2027(e); 7 CFR section 285.2(b)).

For fiscal year 2002 and each fiscal year thereafter, PR may carry forward not more than two percent of its grant for use in the following fiscal year (7 USC 2028(a)(2)(D); Section 4124 of Pub. L. 107-171, 116 Stat. 325-326, May 13, 2002).

**L. Reporting**

**1. Financial Reporting**

- a. SF-269, *Financial Status Report* - Applicable
- b. SF-270, *Request for Advance or Reimbursement* - Not Applicable
- c. SF-271, *Outlay Report and Request for Reimbursement for Construction Programs* - Not Applicable
- d. SF-272, *Federal Cash Transactions Report* - Not Applicable

**2. Performance Reporting - Not Applicable**

**3. Special Reporting - Not Applicable**

**N. Special Tests and Provisions**

**1. EBT Reconciliation**

**Compliance Requirement** - PR must perform all the following:

- a. Record and compare payments to the Daily Activity File and the Daily Payments Summary File prepared by the EBT Services provider for the Department of the Family (PR Annual Plan of Operation, F. Program Administration, b.1.(a), Reconciliation System (EBT)).

- b. Perform the following reconciliations (PR Annual Plan of Operation, F, Program Administration, b.1.(a), Reconciliation System (EBT)):
- (1) Benefits authorized equal benefits posted.
  - (2) Benefits accessed by recipients (net EBT account debits/credits) equal benefit amount transactions approved by the EBT services provider.
  - (3) Net EBT account debits/credits equal amount paid to merchants and financial institutions (plus/minus authorized adjustments).
  - (4) Amount paid to merchants and financial institutions equal funds requested by the EBT services provider (plus/minus authorized adjustments).

PR's EBT service provider maintains transaction trails that document the cycle of household transactions from the posting of point-of-sale transactions at retailers through the settlement of retailer credits. (PR Annual Plan of Operation, E. Criteria for Distribution of Funds, 7. Electronic Benefit Transfer System - EBT Family Card, and F. Program Administration, b.1.(a), Reconciliation System (EBT)).

**Audit Objective** - Determine whether PR performs the required comparisons and reconciliations.

**Suggested Audit Procedures**

- a. Ascertain if PR has a process in place to perform the required comparisons and reconciliations.
- b. Test a sample of comparisons and reconciliations to ascertain if they are properly performed and that there is proper follow-up and resolution of discrepancies.

**UNITED STATES DEPARTMENT OF AGRICULTURE****CFDA 10.568 EMERGENCY FOOD ASSISTANCE PROGRAM (ADMINISTRATIVE COSTS)****CFDA 10.569 EMERGENCY FOOD ASSISTANCE PROGRAM (FOOD COMMODITIES)****I. PROGRAM OBJECTIVES**

The objective of the Emergency Food Assistance Program (TEFAP) Cluster is to provide U.S. Department of Agriculture (USDA) donated commodities to low-income households for home consumption, and to provide hot meals prepared from USDA donated commodities to needy persons in congregate settings.

**II. PROGRAM PROCEDURES**

The Food and Nutrition Service (FNS) of the USDA administers TEFAP. FNS enters into agreements with State distributing agencies for the distribution of USDA donated commodities, and provides funding for the administrative costs these organizations incur in performing this function. The State distributing agencies with which FNS makes agreements for the operation of TEFAP are generally the same State agencies that administer other USDA commodity programs, such as State departments of agriculture, education, etc.

At the local (subrecipient) level, the program is operated by Eligible Recipient Agencies (ERAs). ERAs include public and private non-profit organizations that operate Emergency Feeding Organizations (EFOs), charitable institutions such as hospitals and retirement homes, summer camps for children, and child nutrition programs providing food service, nutrition programs under the Older Americans Act of 1965 (Pub.L. 89-73), and disaster relief programs. EFOs include public and private non-profit organizations that provide nutrition assistance to relieve situations of emergency and distress through the provision of food to needy persons, such as food banks, food pantries, soup kitchens, etc.

An ERA may receive a TEFAP subgrant directly from the State agency, or from another ERA. In designating ERAs, a State agency may give priority to existing food bank networks and other organizations whose primary function is to facilitate the distribution of food to low-income households, including food from sources other than USDA. A State may delegate its storage and distribution functions to one or more food banks or other ERAs.

USDA provides commodities to State agencies, and the State agencies arrange for their delivery to ERAs. State agencies are prohibited from charging ERAs any type of fee for providing this service (7 CFR section 251.9(d); 7 USC 7511). FNS also awards each State agency a cash grant for the administrative cost of carrying out its TEFAP food delivery and oversight functions. The State agency, in turn, awards subgrants to its ERAs and/or incurs administrative costs on their behalf. The value of TEFAP entitlement commodities and the amount of administrative funds a State agency may receive are determined through an allocation formula described at 7 CFR section 251.3(h). USDA may provide bonus commodities in addition to the formula-generated entitlement commodities.

To gain access to its commodities and administrative funds, a State agency must have a distribution plan and a Federal-State Agreement on file with the applicable FNS regional office. The distribution plan gives the State agency's criteria for awarding subgrants to ERAs and for certifying households eligible for TEFAP benefits. Both the Federal-State Agreement and the State agency's agreements with its ERAs may be amended at any time due to program changes or at the request of either party.

Determinations of households' eligibility for TEFAP benefits are generally made by ERAs in accordance with the criteria and procedures established by the State agency in its distribution plan. ERAs may issue commodities to members of eligible households in quantities suitable for meal preparation at home or they may use the commodities in the operation of feeding sites that serve prepared meals.

The ERAs that conduct these issuance and congregate feeding activities are known as "distribution sites." In some cases, distribution sites are operated by separate organizations as sub-subrecipients of other ERAs. Some distribution sites use mostly paid employees to carry out their missions, while others rely heavily on the services of volunteers.

The Personal Responsibility and Work Opportunity Reconciliation Act of 1996 incorporated into TEFAP a previously separate program entitled Commodities for Soup Kitchens and Food Banks (CFDA 10.571). Activities formerly conducted under that program are now deemed TEFAP activities, and residual stocks of commodities originally made available for that program are now deemed TEFAP commodities. Accordingly, CFDA 10.571 should not appear in a State's or subrecipient's Schedule of Expenditures of Federal Awards.

### **Source of Governing Requirements**

TEFAP is authorized by the Emergency Food Assistance Act of 1983 (Pub. L. Law 98-8) (7 USC 7501-16), as amended by the Hunger Prevention Act of 1988 (Pub. L. 100-435) and the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (Pub. L. 104-193). Program regulations are found at 7 CFR part 251.

### **III. COMPLIANCE REQUIREMENTS**

**In developing the audit procedures to test compliance with the requirements for a Federal program, the auditor should first look to Part 2, Matrix of Compliance Requirements, to identify which of the 14 types of compliance requirements described in Part 3 are applicable and then look to Parts 3 and 4 for the details of the requirements.**

## A. Activities Allowed or Unallowed

1. A State agency or ERA must use its administrative cost grant or subgrant for activities intrinsic to the processing, transportation, and distribution of TEFAP commodities within its State or service area. Such activities are listed at 7 CFR section 251.8(e)(1)(i) through (v). Under certain circumstances, a State agency may also use these funds for transporting TEFAP commodities to other States and transporting non-USDA foods in from other States (7 USC 7505(d)).
2. An ERA that receives USDA non-program commodities and TEFAP commodities may use its administrative cost subgrant for the distribution of both classes of commodities. In addition, a State agency or ERA may use its administrative funds for certain activities associated with the distribution of non-USDA foods donated by private individuals and organizations (7 CFR section 251.8(e)(1)).

## B. Allowable Costs/Cost Principles

While regulations issued under previous legislation had required State agencies and ERAs to use TEFAP administrative funds solely for direct costs, the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 expressly identified State level indirect costs as allowable costs (Personal Responsibility and Work Opportunity Reconciliation Act of 1996, section 202A(c)(1)).

## E. Eligibility

### 1. Eligibility for Individuals

- a. *Receipt of Commodities for Household Use* - An EFO certifies households eligible to receive TEFAP commodities for household consumption by applying income eligibility criteria established by the State agency (7 CFR section 251.5(b)). These criteria are approved in advance by FNS as part of the State agency's distribution plan (7 CFR section 251.6(a)).
- b. *Receipt of Prepared Meals* - There is no means test for eligibility of persons receiving prepared meals. Their eligibility is derived from the ERA's eligibility to receive and use TEFAP commodities.

### 2. Eligibility for Group of Individuals or Area of Service Delivery - Not Applicable.

### 3. Eligibility for Subrecipients

To receive commodities and TEFAP administrative funds, a public or non-profit private organization must have entered into an agreement with the State agency, or with another ERA, binding it to perform the duties of an ERA. The State

agency's distribution plan identifies the classes of organizations with which it will enter into such agreements.

## **G. Matching, Level of Effort, Earmarking**

### **1. Matching**

- a. A State agency must match each Federal dollar expended for State-level TEFAP administrative costs with a dollar from non-Federal sources (7 CFR section 251.9(a)).
  - (1) *Exceptions* - The following States are exempted from the matching requirement in any fiscal year in which their respective required matching contributions would have fallen below \$200,000: American Samoa, Guam, the Virgin Islands, and the Commonwealth of the Northern Marianas (7 CFR section 251.9(b)).
  - (2) *Acceptable Matching Contributions* - Acceptable matching contributions include:
    - (a) Cash expenditures by the State agency for allowable State- or local-level TEFAP administrative costs (7 CFR section 251.9(c)(1)); and
    - (b) Certain non-cash contributions. These may include: (i) the value of goods and services specifically identifiable with allowable State administrative costs; (ii) the value of goods and services contributed by the State agency to an ERA, which are specifically identifiable with allowable local-level administrative costs; and (iii) the value of third-party in-kind contributions, provided such contributions support functions meeting criteria stated in the program regulations (7 CFR section 251.9(c)(2)).

### **2. Level of Effort - Not Applicable**

### **3. Earmarking**

A State agency must use at least 40 percent of its TEFAP administrative cost grant for costs that benefit ERAs. The State agency may do this by awarding subgrants directly to ERAs and/or by incurring costs the ERAs would otherwise have had to pay themselves (7 CFR section 251.8(e)(4)).

## **L. Reporting**

### **1. Financial Reporting**

- a. SF-269, *Financial Status Report* - Not Applicable
- b. SF-270, *Request for Advance or Reimbursement* - Not Applicable
- c. SF-271, *Outlay Report and Request for Reimbursement for Construction Programs* - Not Applicable
- d. SF-272, *Federal Cash Transactions Report* - Not Applicable
- e. FCS-667, *Report of the Emergency Food Assistance Program (TEFAP) Administrative Costs (TEFAP) (OMB No. 0584-0385)* - This report captures the status of a State's TEFAP administrative cost grant in a manner that identifies the portions applied to State level costs, costs paid by the State on behalf of ERAs, and costs paid by the ERAs themselves. It thus facilitates the monitoring of a State's compliance with the State matching and 40 percent pass-through requirements (7 CFR section 251.10(d)).

*Key line items* - The following line items contain critical information:

- (1) Line c. - *Net Outlays to Date*
- (2) Line f. - *Total State Agency's Share of Net Outlays*
- (3) Line k. - *Total Federal Share*

**2. Performance Reporting** - Not Applicable

**3. Special Reporting** - Not Applicable

**M. Subrecipient Monitoring**

A State agency must make on-site reviews of ERAs under its oversight and of distribution sites operated by such ERAs, in accordance with its distribution plan. At a minimum, the State agency's annual review coverage must include 25 percent of the ERAs that operate TEFAP as a subrecipient of the State agency and one-tenth or 20 (whichever is less) of the ERAs that operate TEFAP as subrecipients of other ERAs in the State. To the maximum extent practicable, review scheduling should enable State agency staff to observe TEFAP commodity issuance and prepared meal service operations (7 CFR section 251.10(e)).

**N. Special Tests and Provisions**

**1. Accountability for Commodities**

**Compliance Requirement** - Accurate and complete records shall be maintained with respect to the receipt, distribution/use, and inventory of donated foods, including end products processed from donated foods. Failure to maintain records required by 7 CFR

section 250.16 shall be considered prima facie evidence of improper distribution or loss of donated foods, and the agency, processor, or entity is liable for the value of the food or replacement of the food in kind (7 CFR sections 250.16(a)(6) and 250.15(c)).

Distributing and recipient agencies shall take a physical inventory of all storage facilities. Such inventory shall be reconciled annually with the storage facility's inventory records and maintained on file by the agency which contracted with or maintained the storage facility. Corrective action shall be taken immediately on all deficiencies and inventory discrepancies and the results of the corrective action forwarded to the distributing agency (7 CFR section 250.14(e)).

**Audit Objective** - Determine whether an appropriate accounting was maintained for donated food commodities, that an annual physical inventory was taken, and the physical inventory was reconciled with inventory records.

### **Suggested Audit Procedures**

- a. Determine storage facility, processing, and end use locations of all donated food commodities, including end products processed from donated foods. Determine the commodity records maintained by the entity and obtain a copy of procedures for conducting the required annual physical inventory. Obtain a copy of the annual physical inventory results.
- b. Perform analytical procedures, obtain explanation and documentation for unusual or unexpected results. Consider the following:
  - (1) Compare receipts, usage/distribution, losses and ending inventory of donated foods for the audit period to the previous period.
  - (2) If auditing at the State distributing agency level, compare distribution by entity for the audit period to the previous period.
  - (3) If auditing at the ERA level, compare relationship of usage of donated foods to production, meals served, or similar activity reports for the audit period to the same relationship for the previous period.
- c. Ascertain the validity of the required annual physical inventory. Consider performing the following steps, as appropriate:
  - (1) Observe the annual inventory process at selected locations and recount a sample of commodity items.
  - (2) If the annual inventory process is not observed, select a sample of significant commodities on hand as of the physical inventory date and, using the commodity records, "roll forward" the balance on hand to the current balance observed.

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- (3) On a test basis, recompute physical inventory sheets and related summarizations.
  - (4) Ascertain that the annual physical inventory was reconciled to commodity records. Investigate any large adjustments between the physical inventory and the commodity records.
- d. On a sample basis, test the mathematical accuracy of the commodity records and related summarizations. From the commodity records, vouch a sample of receipts, usage/distributions, and losses to supporting documentation. Ascertain that activity is properly recorded, including correct quantity, proper period and, if applicable, correct ERA.

## DEPARTMENT OF AGRICULTURE

### CFDA 10.665 SCHOOLS AND ROADS - GRANTS TO STATES CFDA 10.666 SCHOOLS AND ROADS - GRANTS TO COUNTIES

#### I. PROGRAM OBJECTIVES

The objective of this program is to share receipts from the national forests with the States in which the national forests are situated. Generally, these funds are to be used for the benefit of public schools and public roads of the county or counties in which the national forest is situated.

#### II. PROGRAM PROCEDURES

##### General

Since the early 1900s, the Congress has enacted laws directing that a State or county be compensated for the presence of Federal lands in the State. The compensation may be based on Federal acreage or a county's population, but in most instances, the payments relate to a percentage of the receipts generated on Federal land. Federal laws requiring payments to States, based on national forest receipts, provide the basis and methodology of the compensation payments to the States but allow States to prescribe how the funds are spent for schools and roads in the county or counties in which the national forest is situated. All disbursement transactions are processed through the U.S. Treasury.

##### Program Operation

*25-Percent Payment* - 25 percent of gross receipts generated on Forest Service lands during the fiscal year is distributed to the States. Payments are to be used to benefit public schools and public roads of the county or counties in which the national forest is situated. Two payments are made to the States: an interim payment is made in October on the basis of estimated third-quarter operating results, and a final payment is made in December, providing the balance of the actual receipts due to the counties. The Forest Service calculates both payments and sends letters to the States advising them of the amount and of each county's historic percentage of the payment based on the county's acreage in the national forest. The Forest Service notifies the U.S. Treasury of the amounts to be paid, and the funds are electronically transmitted to the States. The States verify the amount of each deposit with information received from the Forest Service and then they distribute the funds to the counties in which the national forests are situated.

*Full Payment Amount (Secure Rural Schools and Community Self-Determination Payment)* - This payment is made in relation to the State's 25-Percent Payment. Each eligible county elects to receive either its share of the 25-Percent Payment, as described above, or its share of the State's "Full Payment Amount." Such payments are authorized for Federal Fiscal Years (FY) 2001 through 2006. For purposes of making the FY01 payment, the full payment amount for each eligible State, and the share thereof for each eligible county that elects to receive it, is stated in the Forest Service document entitled "Pub. L. No. 106-393, Secure Rural Schools and Community Self-Determination Act," dated July 31, 2001. For purposes of making the

payments required in Federal FYs 2002 through 2006, the Forest Service shall annually adjust the amounts stated in that document in accordance with section 751(b) of Pub. L. 107-76 (115 Stat. 739, November 28, 2001).

*Quinault Special Payment* - 45 percent of the gross receipts generated by the Quinault Special Management Area is distributed to the State of Washington for the benefit of public roads and public schools. This amount is combined with the 25-Percent Payment to Washington State to make one payment. Washington State distributes Quinault payments to the counties as part of its 25-Percent Payment.

*Arkansas Smoky Quartz Payment* - 50 percent of the receipts from the sale of quartz mined on the Ouachita National Forest in Arkansas is distributed to Arkansas for the benefit of public roads and public schools of the counties in which the forest is situated. The Forest Service calculates these payments by subtracting the quartz receipts from the forest receipts and applying the 50 percent rate to these quartz receipts. The quartz payment is added to the State's 25-Percent Payment and distributed in one lump sum.

*Payments to Minnesota* - Three-quarters of 1 percent of the fair appraised value of specified national forest lands in Cook, Lake, and St. Louis Counties is paid to the State. The Forest Service adds this amount to the 25 Percent Payment for the remainder of Minnesota and makes one payment to the State. The State distributes funds to Cook, Lake, and St. Louis counties according to the fair appraised value of the specified national forest lands in each county.

*National Grasslands Payment* - 25 percent of net revenues from national grasslands and land utilization projects (LUPs) administered under Title III of the Bankhead-Jones Farm Tenant Act (grazing receipts collected by the Forest Service and mineral receipts collected by the Minerals Management Service and transmitted to the Forest Service for distribution) is distributed to the 80 counties containing Forest Service national grasslands. Payments are made directly to the counties where the national grasslands and LUPs are located.

### **Source of Governing Requirements**

*25 Percent Fund* - 16 USC 500

*Secure Rural Schools and Community Self-Determination Act Payments* - 16 USC 500 note; Section 751 of Pub. L. 107-76 (115 Stat. 739, November 28, 2001)

*Quinault Special Payment* - Pub. L. 100-638, section 4(b)(2)

*Arkansas Smoky Quartz Payment* - Pub. L. 100-446, section 323

*Payments to Minnesota* - 16 USC 577g and 577g-1

*National Grasslands Payment* - 7 USC 1012

### **Availability of Other Program Information**

Program information may be found on the Internet at <http://www.fs.fed.us>.

### III. COMPLIANCE REQUIREMENTS

**In developing the audit procedures to test compliance with the requirements for a Federal program, the auditor should first look to Part 2, Matrix of Compliance Requirements, to identify which of the 14 types of compliance requirements described in Part 3 are applicable and then look to Parts 3 and 4 for the details of the requirements.**

#### A. Activities Allowed or Unallowed

1. *25-Percent Payment* funds must be used for public roads and public schools of the county or counties in which the national forest is situated (16 USC 500 note section 102).
2. *Full Payment Amount* funds must be used for public roads and public schools of the county in which the national forest is situated (Title I), special projects on Federal lands (Title II), or county projects (Title III) (16 USC 500 note sections 102, 202, and 302).
3. *Quinault Special Payment* funds must be used for public schools and roads of the county or counties in which the national forest is situated (Pub. L. 100-638, section 4(b)(2)).
4. *Arkansas Smoky Quartz Payment* funds must be used for public roads and public schools in the counties in which the Ouachita National Forest is located (Pub. L. 100-446, section 323).
5. *Payments to Minnesota* funds have no restrictions on use (16 USC 577g and g-1).
6. *National Grasslands Payment* funds must be used for roads or schools in the county in which the land is located (7 USC 1012).

#### G. Matching, Level of Effort, Earmarking

1. **Matching** - Not Applicable
2. **Level of Effort** - Not Applicable
3. **Earmarking**

A county that elects to receive its share of the *Full Payment Amount* and that share is \$100,000 or more must:

- a. Use at least 80 percent, but not more than 85 percent of the funds, for public roads and public schools (16 USC 500 note section 102(d)).

- b. Use the balance of the funds for any combination of the following:
- (1) Reserve for special projects on Federal lands in which case the funds are deposited in a special account in the U.S. Treasury (16 USC 500 note sections 102(d), 202).
  - (2) Search, rescue, and emergency services; community service work camps; easement purchases; forest related educational opportunities; fire prevention and county planning; and community forestry (16 USC 500 note sections 102(d) and 302).
  - (3) Return to the U.S. Treasury (16 USC 500 note sections 102(d) and 402).

## UNITED STATES DEPARTMENT OF AGRICULTURE

### CFDA 10.760 WATER AND WASTE DISPOSAL SYSTEMS FOR RURAL COMMUNITIES

#### I. PROGRAM OBJECTIVES

The Water and Waste Program is designed to assist rural communities in obtaining safe drinking water and adequate waste facilities, which are prerequisites for economic growth. In recent years, water and waste systems have been subject to increasingly stringent regulation under the Safe Drinking Water Act and the Clean Water Act. This program is instrumental in providing the financing to build or upgrade rural water and waste facilities.

#### II. PROGRAM PROCEDURES

Under this program, the United States Department of Agriculture's (USDA) Rural Utilities Service (RUS) awards direct loans, loan guarantees, and project grants for new and improved water and waste systems serving rural areas where financing is not available from commercial sources at reasonable rates and terms. The Water and Waste Program is authorized to provide loan and grant assistance to eligible applicants for water and waste disposal facilities in rural areas and towns of up to 10,000 people.

Eligible applicants include: (1) a public body, such as a municipality, district, county, authority, Indian tribe, or other political subdivision of a State, territory or commonwealth (7 CFR sections 1780.7(a)(1) and (a)(3)); or (2) an organization operated on a not-for-profit basis, such as a cooperative, association, or private corporation (7 CFR section 1780.7(a)(2)).

#### **Direct Loans for Water and Waste Disposal Systems**

To establish its eligibility for a loan, an applicant must demonstrate to RUS that it cannot finance the proposed project from its own resources or obtain sufficient credit to do so at reasonable terms or rates. In addition, the applicant must have the legal authority to construct, operate, and maintain the proposed facility, and to give security for and repay the proposed loan. (7 CFR section 1780.7) A loan is repayable in not more than 40 years or the useful life of the facility, whichever is less. Interest is charged at a poverty rate, intermediate rate, or market rate depending on the circumstances (7 CFR section 1780.13).

#### **Project Grants for Water and Waste Disposal Systems**

RUS makes grants in conjunction with direct loans for water and waste disposal projects servicing the most financially needy communities in order to reduce user costs to a reasonable level. Grant amounts are based on a graduated scale that provides higher amounts for projects in communities that have lower income levels; however, a grant amount may never exceed 75 percent of a project's eligible development costs. To establish grant eligibility, an applicant must demonstrate to RUS that it serves a rural area whose median household income (MHI) falls below the statewide nonmetropolitan median household income (NMHI) (7 CFR section 1780.10).

## **Guaranteed Loans for Water and Waste Disposal Systems**

RUS generally guarantees 80 percent of the loan amount but may, in extraordinary circumstances, guarantee a higher level not to exceed 90 percent. The interest rate for guaranteed loans is negotiated between the recipient and the lender (7 CFR sections 1980.819 and 1980.823).

### **Source of Governing Requirements**

The program is authorized by under Section 306 of the Consolidated Farm and Rural Development Act (7 USC 1926). Implementing regulations are at 7 CFR part 1780.

### **Availability of Other Program Information**

RUS maintains a home page on the Internet (<http://www.usda.gov/rus/water/>), which provides general information about this program.

## **III. COMPLIANCE REQUIREMENTS**

**In developing the audit procedures to test compliance with the requirements for a Federal program, the auditor should first look to Part 2, Matrix of Compliance Requirements, to identify which of the 14 types of compliance requirements described in Part 3 are applicable and then look to Parts 3 and 4 for the details of the requirements.**

### **A. Activities Allowed or Unallowed**

1. Loan and grant funds may be expended on eligible project costs, as approved by RUS. These expenditures include items such as land acquisition, water rights, legal fees, engineering fees, construction costs, and the purchase of equipment (7 CFR section 1780.9).
2. Loan and grant funds may not be used for the following (7 CFR section 1780.10):
  - a. Facilities which are not modest in size, design, and cost.
  - b. Loan or grant finder's fees.
  - c. The construction of any new combined storm and sanitary sewer facilities.
  - d. Any portion of the cost of a facility which does not serve a rural area.
  - e. That portion of project costs normally provided by a business or industrial user, such as wastewater pretreatment, etc.
  - f. Rental for the use of equipment or machinery owned by the applicant.
  - g. For other purposes not directly related to operating and maintaining the facility being installed or improved.

**G. Matching, Level of Effort, Earmarking****1. Matching**

Borrowers may be required to provide funds from other sources as required in the grant agreement and the letter of conditions issued by RUS (7 CFR sections 1780.44(d) and (f)).

**2. Level of Effort** - Not Applicable

**3. Earmarking** - Not Applicable

**L. Reporting Requirements****1. Financial Reporting**

- a. SF-269 - *Financial Status Report* - Not Applicable
- b. SF-270 - *Request for Advance or Reimbursement* - Not Applicable
- c. SF-271 - *Outlay Report and Request for Reimbursement for Construction Programs* - Not Applicable
- d. SF-272 - *Federal Cash Transactions Report* - Not Applicable
- e. Form RD 442-2, *Statement of Budget, Income and Equity (OMB No. 0575-0015)* - This report covers financial operations relating to the borrower's water or waste disposal project.
- f. Form RD 442-3, *Balance Sheet (OMB No. 0575-0015)* - This report presents the financial status of the borrower's water or waste disposal project.

**2. Performance Reporting** - Not Applicable

**3. Special Reporting** - Not Applicable

**IV. OTHER INFORMATION***Interim Financing*

After RUS has made a commitment on a loan, the borrower may obtain interim financing from commercial sources (e.g., a bank loan) for the construction period (7 CFR section 1780.30(d)). Expenditures from these commercial sources that will be repaid from the proceeds of the RUS loan should be considered Federal awards expended, included in determining Type A programs, and reported in the Schedule of Expenditures of Federal Awards.

*Status of Outstanding Loan Balance After Project Completion*

In years after the program funds are expended and construction is completed, and the only ongoing financial activity of the program is the payment of principal and interest on outstanding loan balances, the prior loan balances are not considered to have continuing compliance requirements under OMB Circular A-133 § \_\_\_\_.205(d). Prior loans that do not have continuing compliance requirements other than to repay the loans are not considered Federal awards expended and, therefore, are not required to be audited under OMB Circular A-133.

However, this does not relieve the borrower of the requirement to file financial reports on these loans (which are not required to be audited) or otherwise comply with program requirements (e.g., maintaining insurance, depositing funds in federally insured banks, obtaining prior approval for sales of plant).

## UNITED STATES DEPARTMENT OF AGRICULTURE

### CFDA 10.766 COMMUNITY FACILITIES LOANS AND GRANTS

#### I. PROGRAM OBJECTIVES

The objective of the Community Facilities (CF) direct loan, guaranteed loan, and grant programs is to provide direct, guaranteed loan funds or grants to rural communities to construct, enlarge, expand, or otherwise improve essential community facilities in rural communities. Funds are made available to public bodies, non-profit organizations, or federally recognized Indian tribes that are providing essential services to rural communities when financing is not available from other sources at reasonable rates and terms.

#### II. PROGRAM PROCEDURES

These programs are administered at the headquarters level by the United States Department of Agriculture (USDA) Rural Housing Service (RHS) and in the field by USDA Rural Development field offices. Funds are made available directly to local governments, non-profit organizations, and Indian tribal organizations in the form of direct loans, guaranteed loans, and grants. Funds are used for the development of essential community facilities in rural areas and towns of up to 20,000 population.

An essential community facility is one that: (a) supports a function customarily provided by a local unit of government such as a fire and rescue or a health care facility; (b) is a public improvement needed for orderly development of a rural community; (c) does not include private affairs, commercial, or business undertakings (except for limited authority for industrial parks); and (d) is within the area of jurisdiction or operation for the public bodies eligible to receive assistance or a similar local rural service area of a not-for-profit organization owning and operating an essential community facility. A community may be a small city or town, county, or multi-county area depending on the type of essential community facility.

#### **Guaranteed Loans**

The purpose of CF guaranteed loan assistance is to improve, develop, or finance essential community facilities in rural areas. This purpose is achieved through bolstering the existing private credit structure through the guarantee of quality loans which will provide lasting community benefits. Guaranteed loans are loans made by the lender and guaranteed by the RHS. The processing of the loan and requirements placed on the organization receiving the loan are the lender's responsibility.

#### **CF Grants**

Grant funds may be used to assist in the development of essential community facilities in rural areas. Grants are targeted to the neediest communities that meet population criteria for loans and have a median household income below the higher of the poverty rate or 90 percent of the State nonmetropolitan median household income. CF grant funds may not support more than 75 percent of the facility's cost and are based on eligibility criteria and the feasibility of the project.

## **Administration**

RHS authorizes, monitors, and provides funding for administration of CF loans and grants. The USDA Rural Development State, local, district, and area offices monitor and evaluate the progress of the CF programs.

## **Certification**

Eligibility for CF direct and guaranteed loan assistance is based on: (a) the type of organization applying for the loan (public body, non-profit organization, or federally recognized Indian tribe); (b) whether the applicant can demonstrate that it is unable to finance the proposed project from its own resources or from commercial credit at reasonable rates and terms; (c) whether the applicant has authority to develop, own, and operate the proposed facility; and (d) whether the applicant can legally borrow money and make payments on debts obligated.

Grant assistance may be provided to entities located in eligible rural areas with populations of up to 20,000 and where the median household income of the service area is below the higher of the poverty line or 90 percent of the State non-metropolitan median household income. Priority is given to applicants located in communities of 5,000 or less and where the median household income of the population to be served by the proposed facility is below the higher of the poverty line or 60 percent of the State non-metropolitan median household income.

## **Assessing Need**

Applicants must have the legal authority to borrow and repay loans, pledge security for loans, and construct, operate, and maintain the facility. They must also be financially sound and able to organize and manage the facility effectively. Repayment of the loan must be based on tax assessments, revenues, fees, or other sources of money sufficient for operation and maintenance of reserves and debt retirement. Grant assistance is based on the minimum amount sufficient for feasibility of the facility.

## **Source of Governing Requirements**

The program is authorized under the Consolidated Farm and Rural Development Act of 1972. The program laws for CF direct and guaranteed loans are 7 USC 1926(a)(1) and for CF grants 7 USC 1926(a)(19).

Implementing regulations are:

Direct Loans	7 CFR part 1942
Guaranteed Loans	7 CFR part 3575
Grants	7 CFR part 3570.

### III. COMPLIANCE REQUIREMENTS AND SUGGESTED AUDIT PROCEDURES

**In developing the audit procedures to test compliance with the requirements for a Federal program, the auditor should first look to Part 2, Matrix of Compliance Requirements, to identify which of the 14 types of compliance requirements described in Part 3 are applicable and then look to Parts 3 and 4 for the details of the requirements.**

#### A. Activities Allowed or Unallowed

1. *Community Facilities Direct Loans, Guaranteed Loans, and Grants* - Funds may be used to construct, enlarge, or improve essential community facilities providing essential service primarily to rural residents and rural businesses. Examples of essential community facilities are public safety equipment and facilities; health services; community, social and cultural services; transportation facilities such as streets, roads, and bridges; hydroelectric generating facilities; and recreation facilities (guaranteed loans only). Funds are used to pay reasonable fees and costs associated with the loan, interest on loans until the facility is self-supporting, and the costs of acquiring interest in land and rights. Funds may also be used to purchase or lease equipment, pay initial operating expenses, refinance debts, and pay obligations for construction incurred before issuance of conditional commitment. The projects (including costs) are described in a project summary prepared by USDA Rural Development (7 CFR sections 1942.17(d), 3575.24 and 25, and 3570.61(b)).
2. *Unallowed Activities* - Loan funds may not be used to finance: (a) on-site utility systems or businesses; (b) industrial buildings in connection with industrial parks; (c) community antenna television services; (d) electric generation except for hydroelectric or transmission facilities and telephone systems; (e) facilities which are not modest in size, design, or cost; and (f) loan or grant finders fee (7 CFR sections 1942.17(d)(2)) and 3575.24).

#### L. Reporting Requirements

##### 1. Financial Reporting

- a. SF-269, *Financial Status Report* - Not Applicable
- b. SF-270, *Request for Advance or Reimbursement* - Not Applicable
- c. SF-271 - *Outlay Report and Request for Reimbursement for Construction Programs* - Not Applicable
- d. SF-272 - *Federal Cash Transactions Report* - Not Applicable
- e. RD 442-2, *Statement of Budget, Income, and Equity (OMB No. 0575-0015)* - This report covers financial operations relating to the borrower's CF project.

- f. RD 442-3, *Balance Sheet (OMB No. 0575-0015)* - This report presents the financial status of the borrower's CF project.

**2. Performance Reporting** - Not Applicable

**3. Special Reporting** - Not Applicable

#### IV. OTHER INFORMATION

##### *Interim Financing*

After RHS has made a commitment on the loan, the borrower may obtain interim financing from commercial sources (e.g., a bank loan) during the construction period (7 CFR section 1942.17(n)(3)). Expenditures from these commercial loans which will be repaid from a CF loan should be considered Federal awards expended, included in determining Type A programs, and reported in the Schedule of Expenditures of Federal Awards.

##### *Years After Project Completion*

In years after the program funds are expended and construction is completed, and the only ongoing financial activity of the program is the payment of principal and interest on outstanding balances, the prior loan (including loan guarantees) balances are not considered to have continuing compliance requirements under OMB Circular A-133 §\_\_.205(d). Prior loans that do not have continuing compliance requirements other than to repay the loans are not considered Federal awards expended and, therefore, are not required to be audited under OMB Circular A-133.

However, this does not relieve the non-Federal entity to file financial reports (which are not required to be audited) or otherwise comply with program requirements (e.g., maintaining insurance, depositing funds in federally insured banks, obtaining prior approval for sales of the facility).