Audit Report

Troy City School District
School Lunch Fund

For the Period

July 1, 2000 through June 30, 2001

SD-0802-4

March 26, 2003

The University of the State of New York
THE STATE EDUCATION DEPARTMENT
Office of Audit Services
Albany, New York 12234

THE STATE EDUCATION DEPARTMENT / THE UNIVERSITY OF THE STATE OF NEW YORK / ALBANY, NY 12234

Daniel Tworek, Director
Room 524 EB
Tel. (518) 473-4516
Fax (518) 473-0259
E-mail: dtworek@mail.nysed.gov

March 26, 2003

Mr. Armand Reo
Superintendent
Troy City School District
1728 Tibbits Avenue
Troy, New York 12180

Dear Mr. Reo:

The following is our final audit report (SD-0802-4) on Troy City School District's School Lunch Fund for the period July 1, 2000 through June 30, 2001. The audit was conducted pursuant to Education Law Section 305 and the Board of Regents/State Education Department Strategic Plan – Goal #5, which states: "Resources under our care will be used or maintained in the public interest."

Background

In 1996, the Enlarged City School District of Troy (Troy) entered into an agreement with a food service management company (FSMC) to operate Troy's School Lunch Program for the 1996-97 school year. The agreement allowed an annual administrative fee of $15,000 payable by Troy to the FSMC for its services. In return, the FSMC was responsible for the efficient management of the food service program. As part of its agreement with Troy, the FSMC assumed any program deficit and guaranteed a profit of $25,000 to Troy, subject to certain conditions. For example, Troy was responsible for equipment replacement and repair.

Troy and the FSMC extended the 1996 agreement annually through 1999-2000. The 1999-2000 extension shows the administrative fee had risen to $15,872 while the profit guarantee remained at $25,000. According to both Troy and FSMC staff, the agreement was further extended for the 2000-01 school year; however, neither Troy nor the FSMC have provided documentation of this extension.

Scope, Objectives and Methodology

The audit reviewed management practices, records, and documentation related to Troy's payments to the FSMC for the School Lunch Program for the period July 1, 2000 through June 30, 2001. The objectives of our review were to determine whether the FSMC had met its financial obligation to Troy and to assess Troy's controls over the School Lunch Fund. We reviewed Troy's contract with the FSMC; examined the FSMC's invoices, payroll, accounting records, and supporting

documentation, such as supplier invoices and employee timesheets; and interviewed Troy and FSMC management and staff.

Audit Results

Troy began the 2000-01 school year with a $156,976 fund balance in its School Lunch Fund, incurred a $59,544 operating deficit (expenses greater than revenue), and ended the year with a $97,432 fund balance. In fact, the fund balance has steadily decreased since June 1998. The following table shows operating results and fund balance for the five-year period ending June 30, 2001.

Table 1: School Lunch Fund – Five-Year Operating Trends

	Year Ending June 30				
	1997	1998	1999	2000	2001
Revenue	$1,440,425	$1,484,421	$1,587,001	$1,601,343	$1,687,335
Expenditures	1,407,291	1,405,203	1,622,825	1,659,831	1,746,879
Operating Income (Loss)	33,134	79,218	(35,824)	(58,488)	(59,544)
Fund Balance	$172,070	$251,288	$215,464	$156,976	$97,432

Source: Independent Auditor's Reports

Troy's School Lunch Fund incurred operating deficits in each of the last three years shown, even though Troy's agreement with its FSMC required the latter not only to assume any deficit but also guarantee a profit of $25,000 per year. Because certain expenditure items such as equipment replacements and repairs are Troy's responsibility, we could not determine whether the FSMC met its financial obligation to Troy for these years without a more detailed review of both Troy and FSMC records.

We reviewed management practices, records, and documentation for the School Lunch Fund for the year ending June 30, 2001 and found that the FSMC did not meet its financial obligation to Troy. In addition, the audit found that Troy did not implement adequate management controls over its School Lunch Fund or its agreement with the FSMC.

FSMC's Financial Obligation Not Met

The FSMC did not meet its financial obligation to Troy. It submitted invoices for amounts in excess of actual documented costs and did not provide Troy with the full profit guarantee. As a result, the FSMC owes Troy $34,504 for the 2000-01 school year as shown in the following table.

Table 2: Troy's Overpayment to FSMC

	Overpayment
Invoices in Excess of Actual Documented Costs (see Table 3)	$33,304
Profit Guarantee Shortage (see Table 4)	1,200
Total	$34,504

Source: Audit Analysis

Troy Payments in Excess of Actual FSMC Costs

The FSMC submitted monthly invoices to Troy as required by the contract. The invoices covered the FSMC's costs of personnel, product (food and paper), and miscellaneous other costs, as well as a management fee. The audit found the invoices did not represent actual documented personnel costs or the agreed to management fee and that Troy reimbursed the FSMC $33,304 in excess of actual reimbursable costs, as shown in the following table.

Table 3: Troy Payments in Excess of Actual FSMC Costs

Actual FSMC Costs	
Personnel (including benefits) -- per FSMC Payroll Summaries	$884,390
Product (Food and Paper) -- per FSMC general ledger detail	578,657
Management Fee -- per contract extension for 1999-2000	15,872
Miscellaneous -- per FSMC general ledger detail (less OGS warehouse fee)	45,078
Total Costs	1,523,997
Invoice Amounts Paid by Troy to FSMC	1,557,301
Invoice Amounts in Excess of Actual Costs	$33,304

Source: FSMC accounting records (payroll summaries, general ledger detail) and Troy accounting records

Presented below is an analysis of certain expenditure categories.

Personnel - The FSMC submitted various conflicting information in support of its personnel (payroll and fringe benefits) costs. Personnel costs were shown as:

- $925,964 per the invoices,
- $925,898 per a profit and loss statement and general ledger,
- $892,236 ($923,122 less a $30,886 credit) per another profit and loss statement, and
- $884,390 per the payroll summary reports.

The FSMC provided adequate explanations of certain discrepancies between the payroll summary reports and the general ledger. For example, the FSMC reported that certain differences were due to overhead charges, costs of temporary help, payroll accruals, and off-cycle payroll. The FSMC reported that the $30,886 credit on the second profit and loss statement was the difference in the cost of medical insurance benefits offered to employees by the FSMC and the benefits offered at the time

the FSMC's contract agreement with Troy was made. The FSMC did not provide any documentation to support this credit. Because the FSMC has not adequately reconciled the conflicting information, the audit is relying on the payroll records which are deemed the most reliable. In addition, the payroll records correspond most closely to the second profit and loss statement.

Management Fee - Troy's agreement with the FSMC allowed for an administrative fee of $15,872 for general and administrative services for the 1999-2000 school year. Because no contract extension was provided for the 2000-01 school year, we used the $15,872 administrative fee in our calculations. The FSMC, however, billed Troy for a $21,501 management fee.

Profit Guarantee

As part of its contract with Troy, the FSMC agreed to assume any program deficit and to guarantee a profit of $25,000 to Troy. In its final profit and loss statement for the year, the FSMC calculated a $25,000 net profit after total expenditures of $1,545,476 and revenue of $1,570,476. Although the actual profit approximated the $25,000 calculated by the FSMC, actual expenditures and revenue were significantly higher as shown in the following table.

Table 4: Profit/Loss Calculation

Troy Expenditures	
FSMC (see table 3)	$1,523,997
OGS Warehouse Fee	10,213
Other Contractual (non - FSMC)	3,853
Surplus Food	106,690
Materials and Supplies	18,782
Total Expenditures	1,663,535
Total Revenues	1,687,335
Profit/(Loss)	23,800
Profit Guarantee	25,000
Profit Guarantee Shortage (Due to Troy)	$1,200

Source: Table 3 and Troy Accounting Records

Troy's actual profit, exclusive of equipment costs, was $23,800 or $1,200 less than the guaranteed profit amount. As such, Troy is entitled to claim an additional $1,200 from FSMC.

Management Controls Need to Improve

Troy did not have adequate management controls over its School Lunch Program or its contract with its FSMC. For example, as previously discussed, Troy may not have properly extended the contract to cover the 2000-01 school year. Also, Troy did not adhere to or require the FSMC to adhere to

those sections of the previous contract pertaining to financial matters or employees. In addition, the audit identified other opportunities for Troy to improve its controls over the School Lunch Program.

Contract Requirements

Troy's 1996 agreement with the FSMC, allows for annual extensions of up to five years. Troy and the FSMC extended the 1996 agreement annually through 1999-2000. According to both Troy and FSMC staff, the agreement was extended through the 2000-01 school year, although neither Troy nor the FSMC have provided a copy of this extension. The 1996 agreement, as extended through the 1999-2000 school year, contains provisions detailing responsibilities for financial accounting, books and records, and for employees. The audit found Troy did not adhere to or require the FSMC to adhere to these sections of the contract.

Financial Accounting, Books, and Records

The financial accounting, books, and records section of the contract defines requirements for the FSMC to submit monthly and year-end reports, and to maintain accurate books and records to support all allowable expenses. In addition, this section of the contract defines requirements for Troy to audit and approve all FSMC claims for reimbursement, to audit all large expense items (food, labor, and others) quarterly as well as to perform random audits on smaller expense items, and to audit the FSMC's operations as part of its year-end audit.

Although the FSMC submitted monthly and year-end reports, the reports were not accurate and were not adequately supported. For example, personnel costs per the monthly invoices exceeded personnel costs per the revised profit and loss statement by almost $34,000 and exceeded costs per the payroll summary reports by almost $42,000. According to FSMC officials, about $31,000 of the differences were related to excess medical insurance benefits paid to employees but not the responsibility of Troy.

Troy paid the FSMC $33,304 in excess of actual FSMC costs and did not receive the full profit amount guaranteed by the contract. These overpayments may have been prevented if Troy had adequately reviewed FSMC charges. Troy's former Transportation Director performed only a cursory review of the monthly FSMC invoices for reasonableness. He did not review any supporting schedules or documentation. In addition, the Internal Claims Auditor did not review the invoices before approving them for payment. Although the contract required Troy to audit larger expense items quarterly and other items randomly, Troy did not audit any expense items. In fact, Troy only requested supporting documentation for one of the monthly FSMC invoices and did not document any review of the adequacy of that supporting documentation. In addition, Troy did not audit the FSMC's operations as part of its year-end audit.

Employees

The section of the contract pertaining to employees states that Troy and FSMC will mutually agree upon staffing patterns, and FSMC shall provide Troy with a schedule of employees, positions, assigned locations, salaries, and hours to be worked. During the 2000-01 school year, Troy and FSMC did not mutually agree upon staffing patterns, and Troy had no schedule of employees, positions, assigned locations, salaries, and hours to be worked.

The contract also states that FSMC shall not be responsible for hiring employees in excess of the number required for efficient operation of the School Lunch Program. During this audit, the FSMC, after consulting with Troy officials, reduced its workforce 10 percent by releasing two of its five full-time salaried employees and seven of its 84 hourly employees. In addition, the FSMC slightly reduced the hours of the remaining hourly employees. According to Troy and FSMC staff, services to Troy were not compromised by the reduction in workforce. Although the excess staff and hours were apparently not necessary for the efficient operation of the program, Troy was responsible for financing these unnecessary costs.

Other Opportunities for Improvements in Controls

The audit identified additional opportunities for Troy to improve its management controls over the School Lunch Program.

FSMC's personal service costs were not adequately supported by signed and approved timesheets. For example, FSMC employees do not sign their timesheets on a consistent basis, numerous timesheets did not show actual hours worked, and work leaders and the FSMC manager do not approve and sign timesheets.

In order to serve all students, including those who do not have the appropriate applications on file or available cash, the FSMC allows students to charge their meals on account. However, the cashier system is unable to carry a receivable balance greater than $8.75. Student balances remained at $8.75 regardless of how high the balances actually grew. As a result, the FSMC is unable to track actual amounts due from students once the amounts exceed $8.75.

Recommendations

1. Recoup the $34,504 overpayment (as shown in Table 2) to the FSMC for the 2000-01 school year.

2. Determine if Troy overpaid the FSMC for the 2001-02 school year, and recoup any overpayment.

3. Retain copies of all contracts and contract extensions.

4. Adhere to all contract requirements regarding the FSMC's claims for payment including:
   - audit and approve all FSMC claims for payment,
   - audit all large expense items (food, labor and others) quarterly,
   - perform random audits on smaller expense items, and
   - audit the FSMC's operations as part of the year-end audit.

5. Adhere to all contract requirements regarding employees including:
   - reach a mutual agreement with the FSMC on staffing patterns, and
   - require the FSMC to provide a schedule of employees, positions, assigned locations, salaries, and hours to be worked.

6. Require the vendor of the cashier system to correct the system to track and account for receivable balances over $8.75.

District Response

The District did not formally respond to this audit in writing. District officials stated that they have shared the draft report with the District's independent auditor and are working with the FSMC to resolve the issues cited in this report. Further, District officials stated that the status of the School Lunch Fund has improved considerably as a result of steps taken during this audit.

Ninety days from the issuance of this report, District officials will be asked to submit a report on actions taken as a result of this audit. This required report will be in the format of a recommendation implementation plan and it must specifically address what actions have been taken on each audit recommendation.

I appreciate the cooperation and professionalism extended to the audit team during this review.

Sincerely,

Daniel Tworek

Attachment
cc: J. Kadamus A. King, F. O'Donnell, B. Porter, T. Sheldon, C. Foster (DOB), J. Dougherty (OSC), J. Baldwin (Questar III BOCES), P. O'Grady, Board President