

SECTION II – SPECIFIC COMPLIANCE
FUND 60 PROPRIETARY FUNDS

Proprietary funds are used to account for district activities that are similar to business operations in the private sector. They are not used to account for the normal operations of a district regardless as to whether the operations include services provided to outside parties that are offset by revenues such as tuition or adult education fees. There are two categories of proprietary funds -- enterprise funds and internal service funds. The use of these fund types should be consistent with GAAP (GASB Codification 1300.104). Additional guidelines for districts using the internal service fund to account for shared services are outlined *N.J.A.C. 6A:23-2.13*.

There is little change in the proprietary financial statements resulting from GASB 34. Capital Contributions are not reported as a separate component of net assets in the *Statement of Net Assets*, but continue to be reported as such in the funds statements. District staff and auditors should refer to GASB 34, paragraphs 91 through 105 for guidance on proprietary fund financial statements.

Enterprise funds:

Enterprise funds are used to account for operations that are financed and operated in a manner similar to private business operations. The most common examples of enterprise funds in New Jersey school districts are those established to account for the food services program of the district and latchkey programs. **All the expenses of these operations are accounted for in the funds with any board contribution shown as a transfer to cover deficit in the general fund and as an operating transfer in the enterprise fund.**

Auditor's Note – The Transfer to Cover Deficit included in the general fund **must** reconcile to the Operating Transfer – Board Contribution reflected in the enterprise fund. The department has included an edit in the Audsum diskette to identify any discrepancy between the reported amounts and recommends completing the Audsum diskette prior to filing the CAFR. The Transfer to Cover Deficit should be reflected as an Other Financing Use on Exhibit B-2 in the general fund column of the Governmental Funds *Statement of Revenues, Expenditures, and Changes in Fund Balances* and an operating transfer out on the C-1 *General Fund Budgetary Comparison Schedule*.

Food Service – Enterprise Fund

Boards of Education may contract with food service management companies (FSMC) to equip, supply and operate cafeterias without profit to the district pursuant to *N.J.S.A. 18A:33-3*. Every contract for the services of a food service management company should meet federal standards and procurement requirements pursuant to Title 7 of the Code of Federal Regulations pursuant to *N.J.S.A. 18A:18A-42.1*. All districts rebidding their FSMC Contract must rebid pursuant to the Public School Contracts Law, *N.J.S.A. 18A:18A-1 et seq.* as amended.

The most widely used contract method in New Jersey is referred to by the *Accounting Guide for Government Contracts* as the "cost plus a fixed fee (management fee) contract." The food service management company receives a set fee for managing the food service operation and the board is liable for the reimbursement of all costs incurred. Regardless of the contract method, the local board of education is considered the School Food Authority. Federal regulations prohibit contracts that permit all receipts and expenses to accrue to the food service management company. Even if federal reimbursements are not received, schools using management companies and retaining liability for costs incurred are considered the School Food Authority.

As School Food Authorities, daily cash sales and State and Federal reimbursements are school moneys and subject to the State's school laws. Management companies may handle the preparation of food, placing of orders for food and supplies and other associated administrative duties, but they are not permitted under state law to administer or hold school funds.

The following procedures should be implemented in order to comply with state laws for administering school moneys.

1. The income from daily cash sales and State and Federal reimbursements must be under the control of the treasurer of school moneys in any bank or banking institution of this state designated by the board of education as a depository of school moneys. Such funds may be deposited in the Board's general operating account. A separate food service account is not required. (*N.J.S.A. 18A:17-34*)

Receipts and disbursements of food service funds must be separately accounted for in the records of the treasurer and board secretary. The board secretary should maintain the cash records in accordance with *The Uniform Minimum Chart of Accounts (2003 Edition)*.

When the board budgets funds in its general fund budget in account 11-000-310-930, Transfers to Cover Deficit, those funds may be transferred to the Enterprise Fund at the end of the year for the actual amount, if any. If made prior to the end of the year, any amount of the transfer not needed for a deficit may be refunded to the general fund.

2. The board may by resolution designate the board secretary or another person to approve payments without board approval to expedite the payment process. All such payments must be issued on properly signed warrants and subsequently ratified by the board. The board's resolution may limit the authorization to certain purposes such as the school food service reimbursements and may also limit the dollar amount per payment or month. (*N.J.S.A. 18A:19-1, 2, 4 and 4.1*)
3. Loans or advances from the board to a food service management company are prohibited. All claims and demands must state that articles have been furnished or services rendered before payment can be made. (*N.J.S.A. 18A:19-3*)
4. Food service management companies may negotiate the cost reimbursement dates with the board. However, no interest may be charged on payments that are not made within the negotiated dates.
5. The food service management company must provide itemized claims for services and goods to the board secretary for reimbursement.
 - a) The food service management company should process payroll data in such a way that the board secretary can reimburse it in time for payroll checks to be issued. A one-week lag between payroll period and check disbursement should provide sufficient time for all necessary verifications and payments.
 - b) The food service management company must submit an itemized claim for reimbursement for all goods and services. Reimbursement claims for payroll should include either a copy of the company's payroll for those employees providing service to the district or an itemized listing of employees, check numbers and date, hours worked and earnings. In the latter scenario, payrolls and support documentation must be made available whenever requested by the board secretary and for the annual audit.

When the food service management company purchases specifically for the school district, reimbursement claims for goods should list invoice numbers, dates, vendor names and amounts (Sample 1 on page II-60.4). If the food service management company purchases food in bulk for a number of districts, it may use the above method allocating invoice amounts between districts based on the percentage of each district's student enrollment (or participation) to the total enrollment for all schools (Sample 2 in Section II, Chapter 60). It may also use a per-meal cost calculation based on the total amount of the invoices divided by the total meals served to all districts. Each district's pro-rata share of the costs would be the per-meal cost multiplied by the meals served in each district (Sample 3 in Section II, Chapter 60).

When a food service management company submits an itemized claim for reimbursement, it is not necessary to provide vendor invoices. However, they must be made available whenever requested by the board secretary and for the annual audit.

6. The board of education and the food service management company should work closely to minimize the time of reimbursements and to avoid cash flow problems. However, a food service management company may need to establish a line of credit if the timing of reimbursements is not sufficient to make its payrolls. Interest paid is an allowable cost of the contract in such situations.

The foregoing procedures are recommended by the department to comply with the state's statutes for administering school funds. However, these procedures do not replace but rather supplement the requirement contained in 7 CFR 210.16 that all books and records of the food service management company pertaining to the school food service program shall remain the property of the school district. Auditors must include appropriate comments and recommendation in the event that funds are not properly administered as described in Division of Finance Policy Bulletin 200-12.

SAS #70 Reports

In accordance with SAS #70, as amended by SAS #88, school district auditors may evaluate the internal controls of a food service management company by relying upon the opinions of a "service auditor" of the food service management company's internal control system. To that end, school districts must only contract with food service management companies that can provide an audit opinion on said company's system of internal control. Beginning in 1994-95, all food service management company bid specifications, contracts and/or addenda must include this requirement as a condition of bid qualification.

SAMPLE 1

Foodland Food Services
 123 Broad Street
 Anytown, NJ 08000
 609-123-4567

October 15, 200X
 Invoice #123456

New City School District
 Highland Street
 Old Town, NJ 08111

For reimbursement of costs incurred related to the provision of food services for the schools of the New City School District during the month of September 200X. The costs incurred are listed below:

<u>Invoice #</u>	<u>Date</u>	<u>Vendor Name</u>	<u>Amount</u>
06932	8/31/0X	Bakeland	\$2,398.61
12555X	9/02/0X	Murray's Meats	6,779.38
431182	9/03/0X	Polly's Produce	796.54
218812	9/07/0X	Dan's Dairy	877.32
06988	9/07/0X	Bakeland	531.89
12682X	9/07/0X	Murray's Meats	153.90
431906	9/13/0X	Polly's Produce	591.83
219601	9/24/0X	Dan's Dairy	877.32
		Total	<u>\$13,006.79</u>

Please remit the above amount by November 15, 200X. The listed invoices are available for audit and review. I certify that the within invoice is correct in all its particulars, that the described goods or services have been furnished or rendered and that no bonus has been given or received on account of said invoice.

Franklin Chief
 President
 Foodland Food Services

SAMPLE 2 (2 of 2)

NEW CITY SCHOOL DISTRICT FOOD SERVICES ALLOCATION

Invoice #	Date	Vendor Name	New City	Upper	Lower	Middle	Total
			19.7%	14.1%	27.8%	38.4%	100.0%
6932	8/31/200X	Bakeland	\$208.09	\$148.94	\$293.65	\$405.61	\$1,056.29
12555X	9/2/200X	Murray's Meats	689.23	493.31	972.62	1,343.48	3,498.64
431182	9/3/200X	Polly's Produce	176.45	126.29	249.00	343.94	895.68
218812	9/7/200X	Dan's Dairy	632.22	452.50	892.17	1,232.35	3,209.24
6988	9/7/200X	Bakeland	118.77	85.01	167.61	231.51	602.90
12682D	9/7/200X	Murray's Meats	692.86	495.91	977.75	1,350.55	3,517.07
431906	9/13/200X	Polly's Produce	112.21	80.31	158.34	218.71	569.57
219601	7/13/200X	Dan's Dairy	477.38	341.68	673.66	930.52	2,423.24
		Total	\$3,107.21	\$2,223.95	\$4,384.80	\$6,056.67	\$15,772.63

No. of Students Participating	Percentage
New City	630 19.7%
Upper	452 14.1%
Lower	889 27.8%
Middle	1,230 38.4%
Total	3,201 100.0%

SAMPLE 3 (1 of 2)

Foodland Food Services
123 Broad Street
Anytown, NJ 08000
609-123-4567

October 15, 200X
Invoice #123456

New City School District
Highland Street
Old Town, NJ 08111

For reimbursement of the New City school district's pro-rata share of costs related to the shared food services program provided by our company. See the attached per meal cost calculation supporting the amount charged.

For the month of September 200X	
1,598 meals @ \$2.45 meal	\$3,910.60

Please remit the above amount by November 15, 200X. The invoices listed on the per meal cost calculation are available for audit and review. I certify that the within invoice is correct in all its particulars, that the described goods or services have been furnished or rendered and that no bonus has been given or received on account of said invoice.

Franklin Chief
President
Foodland Food Services

SAMPLE 3 (2 of 2)

NEW CITY SCHOOL DISTRICT FOOD SERVICES ALLOCATION

Invoice#	Date	Vendor Name	Invoice Amount
6932	8/31/200X	Bakeland	\$ 2,398.61
12555x	9/2/200X	Murray's Meat	6,779.38
431182	9/3/200X	Polly's Produce	796.54
218812	9/7/200X	Dan's Diary	877.32
6988	9/7/200X	Bakeland	531.89
12682X	9/7/200X	Murray's Meat	153.90
431906	9/13/200X	Polly's Produce	591.83
219601	7/13/200X	Dan's Diary	877.32
		Total	\$13,006.79

<u>School District</u>	<u>No. of Meals</u>	<u>Price/Meal</u>	<u>Amount</u>
New City	1,598	\$ 2.45	\$3,910.60
Upper	1,299	\$ 2.45	3,178.89
Lower	1,243	\$ 2.45	3,041.85
Middle	<u>1,175</u>	<u>\$ 2.45</u>	<u>2,875.44</u>
Total	5,315	\$ 2.45	\$13,006.79

Child Nutrition Program Requirements

The Bureau of Child Nutrition Programs is revising its audit policy regarding the review of School Food Services to comply with OMB Circular A-133 Revised (OMB A-133) published in the Federal Register, June 27, 2003. OMB A-133 was revised to raise the audit threshold for all recipients, including state and local governments, to \$500,000. The provisions of OMB A-133 are effective for fiscal years ending after December 31, 2003.

Districts and their auditors should refer to the sample Proprietary Fund statements (Exhibits B-4, B-5, and B- 6) on the NJDOE web site <http://www.nj.gov/njded/finance/fp/cafr/> . When a district has more than two programs in the Proprietary Fund, combining statements should be prepared. Please refer to the sample format for School Food Service Fund Exhibits F-1, F-2 and F-3 in Financial Reporting for New Jersey School Districts, A Sample Comprehensive Annual Financial Report, The CAFR (issued August 1999) for combining statements. The Proprietary Fund combining statements follow the same format but are labeled Exhibits G-1, G-2 and G-3.

Auditors should report on the condition of the financial transactions and statistical records of the School Food Service Fund, including a review of monthly reimbursement vouchers, meal count records, Edit Check Worksheets, and eligibility applications. **Determine whether there are controls providing reasonable assurance that all meals reported to the state agency for reimbursement are based on accurate counts and are served to eligible children.**

Please Note: Effective with October 2003, monthly reimbursement claims were entered on-line using the Child Nutrition Program’s website via the myNewJersey portal. This on-line system provides payment status, payment logs and a monthly report summarizing meals claimed by site. The auditor may request these reports from the district.

1. Suggested audit procedures to ensure that reimbursement received is supported by source documents.
 - a) ELIGIBILITY APPLICATIONS – Review eligibility applications to evaluate completeness of required information and verify eligibility determination. Form number 63 provides guidance for the application approval process and is available on the NJ Department of Agriculture web site at <http://www.state.nj.us/agriculture/applic/forms/#6> . Any incomplete free or reduced price applications should be placed in the Paid (denied) category, and an overclaim must be assessed on the Schedule of Meal Count Activity. Incorrectly determined applications should be placed in the correct category, and the resulting overclaim/underclaim must be identified on the Schedule of Meal Count Activity. Additionally, audit findings related to the free and reduced eligibility determination must be reported in the Auditor’s Management Report (AMR) in the School Food Service section. Free applications that are not available or incorrectly determined must also be cited as an exception under Demonstrably Effective Program Aid, Early Childhood Program Aid, and Instructional Supplement Aid where applicable.

Eligibility may also have been determined through the Direct Certification Process. Please refer to June 2005 Memo, "Direct Certification for Free Meal/Free Milk Benefits for School Year 2005-2006."

Schools participating in Provision 1 or 2 are not required to collect eligibility applications annually. Please refer to eligibility requirements set forth in the Memo, "Application Process for Provisions 1 and 2".

Eligibility Application: Household Application for Free and Reduced Price Meals and/or Milk. Auditors should verify for the sample selected that the correct eligibility applications have been utilized, fully completed, and properly supported and maintained.

- Effective with school year 2005-2006, single or individual child (eligibility) applications are obsolete. The Household Application for Free and Reduced Price Meals and/or Milk is the only eligibility application in use for this school year. Since a foster child is considered a family of one, he/she should be the only child listed on a separate household application. For example, a family with five children (3 of their own and 2 foster children), is required to complete three household applications – one application inclusive of their own three children, plus individual applications for each for the two foster children.
- Household applications must be maintained centrally. (The Department of Agriculture has strongly recommended that a representative from the Local Educational Agency (LEA) attend a Determining Official Workshop.)
- Household applications must be on letter size paper.
- Eligibility determination of a household application is effective for the entire school year with the exception of an income listed as zero. Zero income applications are placed on temporary status and may be updated as additional documentation is received by the district.
- Income must be listed by the amount received by each household member and the frequency of which the member received the income. Frequency is determined as weekly, every two weeks, twice monthly, or monthly.
- There is a new section on the household application used to identify children who are homeless, migrant or runaway and categorically eligible. LEA's must designate an Educational Agency Liaison for the homeless. This liaison is the only approved source of supporting documentation for the application of homeless, migrant or runaway children.

- b) MEAL COUNT RECORDS - Review meal count records on a school-by-school basis to verify meals claimed on reimbursement claim. Edit Check Worksheet(s) must be completed for every reimbursement claim submitted and the required comparisons made before completing the reimbursement claim. Any meals denied free or reduced priced eligibility should be credited at the paid rate of reimbursement and overclaim/underclaim identified on the Schedule of Meal Count Activity.

A sample Schedule of Meal Count Activity is presented on page III-4.20 of this Audit Program and instructions for completion are as follows:

1. Column one is the program name for which reimbursement is received
2. Column two is the meal category, paid, reduced or free
3. Column three is titled, "MEALS TESTED" if less than 100% of all meals claimed for all programs are examined by the auditor. Title column three, "MEALS CLAIMED" if 100% of all meals claimed for all programs are examined by the auditor
4. Column four is titled "MEALS VERIFIED" and represents the total number of meals for each program that the auditor has examined and classified as properly documented and reimbursable
5. Column five is the difference between columns 3 and 4 for each program
6. Column six is the established per meal reimbursement rate for the audit year
7. Column seven is the over/underclaim calculated as column 5 times column 6 for each program. A net over/underclaim for all meal programs combined is presented at the bottom of column seven

Unsupported reimbursement must be cited as a finding of noncompliance and a financial assessment identified on the Schedule of Meal Count Activity (Overclaim/Underclaim). Provide pertinent detail, i.e. school, month.

2. Verification Regulations issued by the United States Department of Agriculture require pricing sponsors of the National School Lunch and School Breakfast Programs to verify a minimum number of approved applications on file as of October 1st of each school year. Sample selection and verification may begin earlier based on projections done by school officials. The independent auditor's review of eligibility applications should include an examination of the internal verification process and internal sampling records.

- The Sample Selection Method for Internal Verification of Applications is:
 - a) Use all approved applications on file at October 1, 2005 to determine the appropriate sample size and to select the applications for verification. Note that sample size depends on the number of paper applications, NOT the number of children represented.
 - b) The required sample size is the LESSER of:
 1. 3% of all approved applications*, or
 2. 3,000 approved "error prone" applications

*Applications included in the sample must be selected from the pool of "error prone" applications, to the extent possible. If there are not a sufficient number of "error prone" applications to complete the sample, the remaining applications should be randomly selected from the pool of "non-error prone" applications.
 - c) "Error prone" applications are those applications characterized by:
 - Annual income within \$1,200 of the annual income guidelines
 - Monthly income within \$100 of the monthly income guidelines
 - Twice a month income within \$50 of the twice a month income guidelines
 - Every two weeks income within \$50 of the every two weeks income guidelines
 - Weekly income within \$25 of the weekly income guidelines
 - d) Fractional sample size calculations are always rounded upward, increasing the sample size. Example: 340 approved applications are on file at October 1st, 2005. (340 X 3% = 10.2 applications; sample size must be 11).

Note to auditor: Verify that internal verification procedures require that each application selected for internal verification be reviewed for accuracy by district personnel other than by the individual who made the initial approval determination. The auditor should verify that the process used by the district resulted in approved applications being classified in the district records as "approved applications" considered in the internal audit sampling pool as described in (b) above. Verify that incorrectly approved applications discovered during the internal sampling process have been removed from the internal sampling pool of "approved applications"; the eligibility status changed, a formal notification sent to the family of a change in eligibility along with instructions for resubmission of their application including information regarding acceptable forms of income documentation in support of their application.

All internal verification activity must be completed by November 15 of each school year. The School Food Authority (SFA) must electronically report the results of their verification activities to the Bureau of Child Nutrition Programs by March 1, 2006. Failure to complete verification will result in reimbursement being withheld by the Bureau. The auditor's review of eligibility applications should include a review of the verification files to ensure that the verification process was completed on a timely basis.

3. Expenditures of school food service revenues should be limited to allowable school food service direct and indirect costs. Review vendor invoices and verify labor costs. Determine that inventory records on food and supply items are currently maintained. Review time sheets and verify labor cost. Verify that payroll records are maintained.
4. Net cash resources may not exceed three months average expenditures. In the event that net cash resources exceed three months average expenditures for the School Food Authority's nonprofit school food service, the State Agency may require the School Food Authority to reduce children's prices, improve food quality or take other actions designed to improve the nonprofit school food service. (REF 7CFR 210:15)

Net cash resources are defined as all monies that are available to, or have accrued to a School Food Authority's nonprofit school food service at any given time, less cash payable. Such monies may include, but are not limited to, cash on hand, cash receivable, earnings on investments, cash on deposit and the value of stocks, bonds or other negotiable securities.

5. The auditor should comment on whether Food Distribution Program (formally U.S.D.A.) commodities were received. If the school district is utilizing a vendor to provide meals, review evidence that the market value of Food Distribution Program donated commodities was credited on monthly invoice statements.
6. Auditors should verify that financial arrangements and other provisions in the Food Service Management contract have been complied with; if not, cite exception.
7. The United States Department of Agriculture does not permit increases in reimbursement for revised vouchers received after 60 days without proper verification. However, payment can be considered if the underclaim is verified in an audit or administrative review. **Auditors are instructed to verify any underclaims (identify in the Schedule of Meal Count Activity) as a result of late revisions.** Please note that such payment is subject to approval.
8. The following memorandums and attachments for the school year 2005-06 are available at local school district offices to be referenced by the auditor:
 - a) March 1, 2005 – SFAs Considering Employing a FSMC for School Year 2005-06
 - b) March 1, 2005 – SFAs Renewing FSMC Contracts for 2006
 - 1 - Index rates/fees
 - 2 - Early Approval of Food Service Management Company (FMSC) Addendum
 - 3 - Directory of Registered Food Service Management Companies
 - c) March 2005 – Child Nutrition and WIC Reauthorization Act: Policy Implementation and Information Sessions
 - d) 2005 Seamless Summer Option Application Documents
 - e) June 2005 - Direct Certification for Free Meal/Free Milk Benefits for School Year 2005-06

- f) June 2005 – School Year 2005-2006 School Nutrition Programs Application Packet Materials
- g) June 2005 - Allowable Costs for Meals in Accordance with N.J.A.C. 6A:23-4.5(a)(20)
- h) July 2005 – Fiscal Year 2006 Verification Workshop Schedule/Guidance (Forms #273/273)
- i) July 2005 – Annual Application Process for Provisions I and II
- j) August 2005 - Public Reimbursement Rates for Child Nutrition Programs/Maximum Meal and Milk Prices
- k) November 14, 2005 – Food Service Privatization: Securing FSMC Contracts
- l) January 2006 – After School Snack Program, On-Site Review
- m) January 2006 – **Revised** Annual National School Lunch Program On-Site Review
- n) February 2006 – Verification Summary Report

FISCAL YEAR 2006
 JULY 1, 2005 – JUNE 30, 2006
 REIMBURSEMENT RATE BREAKDOWN

NATIONAL SCHOOL LUNCH RATES

REGULAR RATE			
SFA's w/less than 60% of Free and Reduced Lunch			
	FEDERAL	STATE	TOTAL
FREE	2.32	0.10	\$2.42
REDUCED	1.92	0.10	\$2.02
PAID	0.22	0.04	\$0.26

HIGH RATE (EXTRA 0.02 CENTS)			
SFA's w/more than 60% of Free and Reduced Lunch			
	FEDERAL	STATE	TOTAL
FREE	2.34	0.10	\$2.44
REDUCED	1.94	0.10	\$2.04
PAID	0.24	0.04	\$0.28

SCHOOL BREAKFAST PROGRAM

REGULAR RATES			
	FEDERAL	STATE	TOTAL
FREE	1.27	0.10	\$1.37
REDUCED	0.97	0.10	\$1.07
PAID	0.23	0.10	\$ 0.33

SEVERE NEED RATES			
	FEDERAL	STATE	TOTAL
FREE	1.51	0.10	\$1.61
REDUCED	1.21	0.10	\$1.31
PAID	0.23	0.10	\$ 0.33

AFTER SCHOOL SNACKS

AT RISK/ AREA ELIGIBLE	0.63
NON- AREA ELIGIBLE	
FREE	0.63
REDUCED	0.31
PAID	0.05

SPECIAL MILK PROGRAM

FREE	Average cost per half pint * Based on Individual SFA's costs
PAID	0.155

Commodity Value \$ 0.175

***SFA'S=SCHOOL FOOD AUTHORITIES**