# Section 10000

## Processing

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10100 Introduction

Each year, the U. S. Department of Agriculture (USDA) buys some ready-to-use food items, such as canned fruits and vegetables. Other USDA Foods purchases, such as frozen whole turkeys, are more difficult to use and many recipient agencies (RAs), primarily school food authorities (SFAs), have turned to the food processing industry to convert hard-to-use USDA Foods into more convenient and usable forms called end products.

USDA Food processing helps RAs economize on food costs through a discount in the normal commercial price or a refund from the processor.

In addition, processing benefits RAs by reducing food preparation time and outlays for equipment, making the most efficient use of USDA Foods, providing more varied and higher quality meals, reducing waste in the food preparation process and stabilizing costs through portion control.

Processors arrange, with RAs or processing cooperative coordinators, to deliver end products:

- To the state-contracted warehouse¹,
- Directly to the RA,
- To an agreed upon storage facility, or
- Via a full line distributor (when utilizing a substitution program).

For the most current information about processing, see the USDA website http://www.fns.usda.gov/fdd/processing/default.htm. You can also find USDA policy memoranda for processing at http://www.fns.usda.gov/fdd/Policy/cp_policies.htm.

10200 Participation

To participate in USDA Foods processing, an RA must have an approved Food and Nutrition Division (FND) Commodity Agreement and sufficient commodity dollars for the pounds committed to processors.

¹ See Food Distribution Program Handbook, Section 14000, Terms, Definitions, and Acronyms for a definition of this term.
Most RAs participate as members of a USDA Food processing cooperative. However, some RAs large enough to handle a truckload of a single USDA Food can process without being a member of a co-op.

10300 Submit Requests in Pounds, Not Cases

Since the USDA only ships USDA Foods in truckload quantities, RAs submit requests for further processing in pounds, not cases.

**EXAMPLES:** A truckload of ground beef is 40,000 pounds. RAs that are members of a processing cooperative must collectively commit 40,000 pounds to make up the truckload. SFAs large enough to process on their own commit the entire 40,000 pounds for further processing.

RAs participating as members of a processing cooperative must submit further processing requests to the Texas Department of Agriculture (TDA) through their cooperative coordinators. The coordinators enter USDA Food pounds into the Texas Unified Nutrition Programs System (TX-UNPS)\(^2\) for each cooperative member.

10400 Approved Processors

RAs wishing to process USDA Foods must use processors approved by TDA. TDA periodically provides cooperative coordinators and direct ship SFAs with a list of approved processors. Processors must have one of the following agreements with TDA:

- Approved state processing agreement, along with a national agreement with USDA that allows the processor to do business with more than one state; or
- Approved master processing agreement for processors only processing in Texas.

10500 TDA Processing Contracts

An RA may employ a processor that has a:

- Master agreement with TDA; or
- State participation agreement with TDA.

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\(^2\) See *Food Distribution Program Handbook*, Section 14000, *Terms, Definitions, and Acronyms* for a definition of this term.
Master agreements are for one year, but can be extended for two additional one-year periods. State participation agreements are renewed each year by TDA.

An RA’s separate agreement with a processor must conform to all federal and state requirements.

NOTE: Some food service management companies (FSMCs) that are employed by RAs to manage part or all of their food service operation must contract with TDA as processors. Though they are not required to contract as processors, some nonprofit organizations (NPOs) that are employed by RAs to provide food service are subject to certain provisions of processing regulations. TDA determines the status of FSMCs and NPOs employed by Food Distribution Program (FDP) contracting entities that are charitable institutions and nonprofit summer camps for children.

**10600 Value Pass-Through Systems**

CEs can choose from four value pass-through systems to purchase end products at a reduced price.

<table>
<thead>
<tr>
<th>Federal Term</th>
<th>Common Term</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discount System</td>
<td>Direct Discount</td>
<td>An RA purchases end products directly from a processor at an established wholesale price minus the contract value of the USDA Foods contained in the end products.</td>
</tr>
<tr>
<td>Refund System</td>
<td>Direct Refund</td>
<td>An RA purchases a processor’s end products and receives from the processor a payment equivalent to the contract value of the USDA Foods contained in the end products.</td>
</tr>
<tr>
<td>Hybrid System</td>
<td>Indirect Discount/Refund –or– Net Off Invoice (NOI)</td>
<td>A processor sells end products containing USDA Foods to a distributor at a gross price. The distributor sells that product to an eligible RA at the commercial price plus delivery costs minus the value of the USDA Foods. The distributor submits a velocity report to the processor, as a rebate application, for the value of the USDA Foods discounted to the RA.</td>
</tr>
<tr>
<td>Alternative Value Pass-Through System</td>
<td>Alternative Value Pass-Through System</td>
<td>A processor submits a request for approval to use an alternate method to pass to the RA the value of the USDA Foods contained in each unit of end product. This system must be approved by FNS at the request of TDA.</td>
</tr>
</tbody>
</table>
10700 Other Systems

10710 Fee-For-Service

Under this system, a processor's bid price (charged by pound or by case) includes the processor's costs of ingredients other than USDA Foods (for example, labor, packaging, overhead and other costs of converting USDA Foods into the specified end product).

10720 Fee-for-Service Billing Methods Through a Distributor

Current processing regulations allow two types of billing arrangements when distributors deliver fee-for-service (FFS) processed end products to RAs.

- An RA may be invoiced by the processor for the FFS and separately by the distributor for delivery and storage.

Or

- The processor may arrange for delivery through a distributor on behalf of the RA. The invoice from the processor includes separate, identifiable charges for the FFS and distributor's charge.

In order to bring the delivery of processed USDA Foods more in line with commercial distribution practices, distributors may charge RAs a total case price.

The following requirements must be met in order to implement this billing method:

- There must be a written assignment from the processor to the distributor as the billing agent: Total case price = fee-for-service contract price + delivery and storage charges.
- The distributor details, in writing, distribution fees to each RA so the RA can identify what the total price represents on the invoice.
- The processor must provide a list of all recipients and case allocations eligible for FFS pricing to distributors; TDA; and USDA upon request.
- Processors retain the financial obligation for sales to ineligible recipients. The commercial distributor\(^3\) cannot assume this obligation. The processing agreement is between the processor, TDA and/or USDA.

\(^3\) See Food Distribution Program Handbook, Section 14000, Terms, Definitions, and Acronyms for a definition of this term.
10730 Child Nutrition Labeling Program

The USDA Agriculture Marketing Service (AMS) evaluates formulations submitted by processors to determine what contribution a serving of the product makes toward the Child Nutrition Program meal pattern requirements. When approved, a label (commonly known as Child Nutrition (CN) label) is attached to the end product stating the product meets USDA specifications and can be credited as a component(s) of the reimbursable meal pattern requirement.

The recipient agencies, not TDA, request processors to obtain a CN label.

10740 U.S. Department of Agriculture (USDA) Processing Contracts

The processing agreement permits the company to receive USDA Foods to process into end products, but it does not establish the price, which the RA pays. The procurement procedures used by the RA should establish the price to be paid by the RA for all USDA Foods, including those end products containing USDA Foods. The RA, as a purchaser, has the responsibility to evaluate prices received and to determine the successful bidder.

Three prices should be included for approved end products containing USDA Foods, which will be purchased under the discount system:

- The gross price (without USDA Foods),
- The value of USDA Foods, and
- The net price.

The USDA Foods value should be compared to the End Product Data Schedule (EPDS) in the processing agreement to ensure accuracy.

In no event should the value of USDA Foods be less than that shown on the EPDS in the processing agreement. On FFS purchases, the fee should not exceed that shown in the processing agreement.

As part of the procurement activity, the RA should ensure that acquisition of an end product containing USDA Foods is cost effective. Determining cost effectiveness is a simple process, but extremely important in demonstrating good management and ensuring that maximum benefits are obtained from the resources expended.

To determine if purchasing a particular end product containing USDA Foods is cost effective, the RA should perform the following steps:
1. Add the value of USDA Foods contained in the end product to the cash (net) price to arrive at the total cost of the item.
2. Obtain gross prices (without value of USDA Foods) for the same and comparable products being sold in the area. (NOTE: Delivery charges and all other costs should be included.)
3. Compare the total cost of the item being considered with the cost data obtained.
4. If the cost of the item (including the value of USDA Foods) being considered is approximately the same as the others, then it can be considered cost effective. However, if the total cost (including the value of USDA Foods) of the item being considered is significantly higher, then it is not cost effective.

10750   End Products and Selection of Processors

TDA will provide to the RA relevant information each year concerning processing agreements approved by both TDA and USDA. The RA uses the information to determine which products to use and which processor(s) to select. TDA updates the information throughout the year as changes are made. The information will, at a minimum, include the following:

- Name of processors;
- Description of the approved end products and any identification codes;
- USDA Foods used in each end product; and
- Portion size.

10760   Value of USDA Foods

The value of USDA Foods contained in a case of end product is determined by multiplying the quantity of each USDA Food by the established price per pound. This per-case net price is identified in the processing agreement on the EPDS for each approved item.

A processor must also list on the EPDS any value credits for byproducts (such as buy-back parts and byproducts like bones, broth, etc.) resulting from processing USDA Foods.

10770   Procurement Standards

When purchasing foods for use in food service programs, the RA must comply with federal, state and local procurement standards. The primary purpose of these standards is to assure that open and free competition exists to the maximum extent possible. The fact that TDA or USDA enters into an agreement with a company to process USDA Foods does not remove the RA’s responsibility to comply with the procurement standards. FDP contracting entities are prohibited from awarding contracts to any entity that develops or drafts procurement documents. FDP contracting entities cannot allow any entity bidding for a contract award to develop:
• Specifications,
• Requirements,
• Statements of work,
• Invitations for bids,
• Requests for proposals,
• Contract terms and conditions, and
• Other procurement documents.

FDP contracting entities must draft their own specifications and procurement documents. Any FDP contracting entity\(^4\) that copies a list of features or evaluation and ranking criteria drafted by a potential vendor and then permits that potential vendor to submit a bid has violated both federal and state procurement regulations.

It is understood that FDP contracting entities have broad discretion in gathering information for use in connection with procurements, any information from potential bidders must be appropriately modified to develop tailored specifications; otherwise, these bidders must be excluded from competing for such procurements. This is to ensure objective contractor performance and eliminate unfair competitive advantage.

**EXCEPTION:** If the FDP contracting entities chooses to use a vendor's information or assistance in developing procurement documents and the vendor is allowed to compete for the award, then the FDP contracting entity must not use any FDP funds for the resulting award.

### 10780 Protest

Any action that diminishes open and free competition undermines the integrity of the procurement process and may subject the FDP contracting entity to bid protests. Therefore, FDP contracting entities must have protest procedures in place to handle and resolve disputes relating to procurements, and must disclose information regarding a protest to TDA.

If TDA determines that you have not complied with procurement requirements, you will be required to take corrective action. If corrective action is not taken, this may result in adverse action up to and including termination of your FDP contract.

\(^4\) See *Food Distribution Program Handbook*, Section 14000, *Terms, Definitions, and Acronyms* for a definition of this term.
10800   Excess Inventory at Processors

Carryover inventory is unused USDA Foods inventory from the previous school year. Carryover inventory is a factor contributing to excess inventory at processors. Excess inventory is defined as stored USDA Foods that exceed a six-month supply.

Federal regulations state that excess inventory must not exceed six months. Contracting entities (CEs) should use all USDA Foods diverted to a processor during the school year to minimize excess inventory and to receive the full benefit of the donated foods.

If a CE is unable to use all the USDA Foods they diverted to a processor in the school year, CEs will have until November 30 of the following school year to use the carryover inventory.

EXAMPLE: If CE123 has USDA Foods left over at a processor from the 2012-2013 school year, CE123 has until November 30 of the 2013-2014 school year to use the USDA Foods.

The processor’s June Monthly Performance Report (MPR) shows carryover inventory. To track carryover inventory, processors must submit via email (CommodityOperations@TexasAgriculture.gov) the following information in an Excel file to TDA with their June MPR:

- Names of CEs with June carryover inventory of USDA Foods,
- USDA Material Numbers and ending balances (in pounds), and
- Average monthly usage for each CE during the school year ending June 30.

Any balances listed as of June 30 is carryover inventory that must be used by November 30. After November 30, excess carryover inventory for each CE is calculated as follows:

June Carryover inventory – Total Inventory Used = Unused Carryover inventory

Example: 10,000 (June carryover inventory) - 5,000 (total inventory used) = 5,000 (unused carryover inventory)

<table>
<thead>
<tr>
<th>June Carryover inventory</th>
<th>Inventory Used</th>
<th>Unused Carryover inventory</th>
</tr>
</thead>
<tbody>
<tr>
<td>10,000</td>
<td>-</td>
<td>5,000*</td>
</tr>
</tbody>
</table>

*If this number is zero or a negative, the CE has used all carryover inventory.

See Food Distribution Program Handbook, Section 14000, Terms, Definitions, and Acronyms for a definition of this term.
To comply with excess inventory regulations, by December 15th processors must transfer all carryover inventory that has not been used by CEs to the State Account and update their tracking systems (e.g., K12, ProcessorLink, etc.). Processors must submit via email (CommodityOperations@TexasAgriculture.gov) the following information in an Excel file to TDA:

- Names of CEs with June carryover inventory of USDA Foods,
- Amount of June carryover inventory by CE,
- Total inventory used as of November 30 by CE,
- Amount of carryover inventory transferred to the State Account for each CE.

TDA will notify co-ops and non co-op schools when this process is complete for each processor.

By January 15, TDA will
- Reallocate carryover inventory in the State Account to CE’s who need the inventory, or
- Use the inventory for future USDA Food orders.

Priority for reallocated inventory is given to CEs that need more inventory to complete the school year and have less than six-months of inventory.

**Exception:** If a CE provides supporting documentation to TDA via email (CommodityOperations@TexasAgriculture.gov) by January 15th, (i.e., data from tracking system displaying an increase in average monthly usage between July and November, or a special circumstance that will be resolved in the second half of the school year) all, or part, of their unused carryover inventory will be returned to their account. The carryover inventory returned to the CE must be used by June 30th. If not, the remaining returned balance will be removed back to the State Account.

To prevent loss of inventory and entitlement dollars, CEs should order product only in amounts needed that can be efficiently used during the school year. CEs should project carryover inventory when submitting new requests for the new school year. Processors should deny new requests when a CE has excess inventory of a product.

TDA may also reduce or reject a USDA Foods request for processing if a CE or processor has inventory in excess of six-month for the USDA Food item.
10900  **Electronic Receipting**\textsuperscript{6} for USDA Foods

Direct ship CEs and CEs that are part of a warehouse co-op for direct shipments of USDA-Foods must receipt electronically into TX-UNPS within 24 hours for each USDA Foods shipment received. Warehouse co-op CEs must have a representative who receipts for shipments in TX-UNPS. CEs serviced by a state-contracted warehouse do not receive direct shipments of USDA Foods and therefore do not receipt into TX-UNPS.

TDA must then receipt electronically into the USDA’s Web-based Supply Chain Management (WBSCM)\textsuperscript{7} system within 24 hours. The entire receipting process, including CE and TDA responsibilities, must be complete within 48 hours.

This requirement applies to all \textbf{direct} shipments of USDA Foods. USDA requires shipment receipts to be entered within 48 hours in order to meet contractual requirements and to provide prompt payment to vendors.

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\textsuperscript{6} See \textit{Food Distribution Program Handbook}, Section 14000, \textit{Terms, Definitions, and Acronyms} for a definition of this term.

\textsuperscript{7} See \textit{Food Distribution Program Handbook}, Section 14000, \textit{Terms, Definitions, and Acronyms} for a definition of this term.