

School Foodservice – Outsource or Self-Op?

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Please note that this study was published before the implementation of Healthy, Hunger-Free Kids Act of 2010, which went into effect during the 2012-13 school year, and its provision for Smart Snacks Nutrition Standards for Competitive Food in Schools, implemented during the 2014-15 school year. As such, certain research may not be relevant today.

School foodservice is one of the most complex departments in a school district. For a variety of reasons, some school districts have turned to private foodservice management companies to assume responsibility for these programs. The decision to outsource foodservices should not be made lightly, as it may or may not be in the best interest of the school district or its students. This paper discusses the question of outsourcing, and it presents pros and cons for both self-operation and privatization. It lays out legal arguments and identifies concerns that school boards must address in order make effective decisions. Finally, it provides guidance in helping districts work through the decision-making process.

Providing high-quality education that prepares children to compete for jobs in a global economy allows them to function in a society that requires more brain and less brawn, and it provides for a multi-cultural experience that is a difficult challenge for school districts today. The No Child Left Behind (NCLB) Act is a legislative mandate for schools to improve student performance or risk losing federal funding. Success as defined by NCLB is measured by standardized testing that assesses student learning against standards of learning. Schools that do not continuously improve student performance may be deemed as failures. Schools failing to meet the standards of NCLB face significant consequences that impact staff and budget.

While enormous resources are being targeted toward academic achievement, today's parents demand a full array of curricular and extra-curricular activities to enhance their children's experiences. In addition, schools must provide a broad range of services for children with developmental and physical challenges, as well as address a variety of needs for the whole child. Often, schools provide these services at a financial cost that affects resources earmarked for academic achievement initiatives.

Is it any wonder that some school boards look at non-academic services, seeking to evaluate the most efficient ways to provide maintenance, transportation, and foodservice? Is it the best use of resources to continue to provide services within district operations, or is it wiser to outsource these programs to a contractor? There are no correct answers to these questions, as every school district's environment is unique. Some issues considered in the decision-making process are operational, and some are more philosophical and/or political in nature. It is important for school board members to make informed decisions based on a careful analysis of the facts and circumstances surrounding their unique situation. Either conclusion, to maintain a self-operated foodservice program or to outsource the service, offers opportunities for success.

Applicable Statutes and Regulations

The federal National School Lunch Program (NSLP) was enacted in 1946. The authorizing statutes are the Richard B. Russell National School Lunch Act and the Child Nutrition Act of 1966 as amended in 2004 (hereafter referred to as "the Acts"). Implementing regulations for the Acts can be found in Title 7 of the Code of Federal Regulations, parts 210-299 (USDA, 2003). Two sections of the regulations are of particular relevance in discussing the contracting of

foodservices: 7 CFR § 210.14, resource management, and 7 CFR § 210.16, food service management companies.

With these regulations in mind, a school board needs to address the role its school foodservice program plays in meeting the district's mission. *Fit, Healthy and Ready to Learn* (Bogden & Vega-Matos, 2001), the authoritative set of policy recommendations for a comprehensive school health program, was developed by the National Association of State Boards of Education. The guidelines state:

"[The] foodservice program shall aim to be financially self-supporting. However, the program is an essential educational and support activity and budget neutrality or profit generation must not take precedence over the nutritional needs of students" (Bogden & Vega-Matos, 2001).

Questioning the Justification for Foodservice Management Companies

While school boards ask if it is the best use of resources to continue the services within district operations, a corollary question would be whether a for-profit enterprise, such as a foodservice management company (FSMC), meets the regulatory requirement that "revenues received by the nonprofit school foodservice are to be used only for the operation or improvement of such food service." (USDA, 2003) Put another way, would the fees taken by an FSMC be better invested in corporate stockholders or in the schools' in-house foodservice program so that it can provide nutritious meals for the students? In response to this question, the regulation states:

"Contracts that permit all income and expenses to accrue to the food service management company and 'cost-plus-a-percentage-of-cost' and 'cost-plus-a-percentage-of-income' contracts are prohibited. Contracts that provide for fixed fees such as those that provide for management fees established on a per meal basis are allowed." (USDA, 2003)

Simply stated, the fixed-fee rate per meal charged by an FSMC for administering the food program is a cost of the program. If the FSMC is able to operate the program more efficiently than a self-operated program, the resulting lower net costs of operation may be justified.

The most current data concerning school foodservice financial performance can be found in a Government Accountability Office report that compared revenues and expenses in 2001 versus 1996-97 (Brown et al., 2003). The GAO found that revenues had declined and expenses had increased, resulting in "a small but increasing shortfall." Another GAO study comparing self-operated school foodservice programs to those administered by a foodservice management company found:

"Nineteen percent of the food authorities reported that they were operating at a deficit after contracting with a foodservice company, about the same percentage reported by food authorities not using these companies in school year 1995-96. In addition, the food authorities with foodservice contracts reported increased student participation in the lunch program; however, participation is still below the level for food authorities that did not use these companies — 49% compared with an estimated 65% to 68%." (Slomba et al., 1996)

Unlike other departments in a school district, the foodservice program is substantially self-contained, generating its own revenue through federal and state reimbursements and cash sales. Foodservices operate under a traditional business accounting, profit and loss (P&L) protocol, rather than through a fund allocation approach common in school accounting. When preparing its annual budget, a district can project its revenue based on the per student allocation from the county or state and control costs by adjusting class size or limiting salaries. The foodservice program, on the other hand, has costs that can and will vary throughout the year, due to changes in the costs of goods and participation levels. In commercial P&L models, a business can raise prices when costs increase; in schools, however, meal prices are more difficult to change. For federally reimbursable meals, the reimbursement rate is fixed by federal law and the school board is responsible for making the decision to raise prices for the student-paid portion of full-price meals. Additionally, school meal consumers, which include both students and parents, are particularly price sensitive.

Labor

In discussing the underlying issues behind outsourcing foodservice operations, a frequent comment is that districts tend to negotiate labor agreements that the foodservice department cannot support. Most districts determine wage increases for all employees based on calculations of projected revenues, but this approach only considers the general fund's labor costs and not the foodservice program's labor costs. Foodservice revenues are likely to be more volatile, responding to a number of factors ranging from unexpected weather to non-student days to field trips, and a program's budget may not support the labor cost increases.

Compounding the labor issue is that school districts, unlike most commercial enterprises, cannot easily make staffing adjustments to meet economic or operational changes. A reduction in force is an unpleasant process and school districts try to avoid this, if possible. Some districts find that they have foodservice staff and salaries that are not sustainable, and there is no easy way to adapt to changing circumstances. When it comes to reducing staff size, controlling the hours worked, and maintaining manageable wage levels, outsourcing the program can shift responsibility from the district to the contractor. Nonetheless, the quality, efficiency, and effectiveness of the school foodservice program reside with the local staff. Even when a district elects to contract with an FSMC, the caliber of local staff is the major determinant of success. Frequently, a management company hires existing personnel to fill staff positions and provides part-time oversight of a district manager who has access to the resources of the company.

Operational Responsibility for the School District

Outsourcing the foodservice program does not relieve the school district of its oversight responsibilities. Federal regulations identify the district's responsibilities when it chooses to contract an FSMC (USDA, 2003). These include a responsibility to:

- Adhere to the procurement standards, as specified in Sec. 210.21, when contracting with an FSMC;
- Ensure that the foodservice operation is in conformance with the school food authority's (SFA) agreement under the program;
- Monitor the foodservice operation through periodic onsite visits;
- Retain control over meal price, and the quality, extent, and general nature of its foodservice; and

- Retain signature authority on the state agency school food authority agreement, free and reduced-price policy statement, and claims.

A report by the U.S. Department of Agriculture (USDA) cites a significant number of cases where this requisite oversight was not executed.

"Finally, we found that SFAs turned over most aspects of their programs, including meal accountability, to the management companies. There was little or no SFA oversight. In all, 16 of the 24 SFAs we visited did not have adequate controls in place to ensure accurate meal claims or to prevent management companies from being reimbursed for non-program costs" (USDA, 2002).

The USDA report does not imply that a school board should not consider outsourcing its foodservice operation; however, the district must have a system in place to ensure full compliance with the law, as well as be responsible for the quality of the program being offered. The district is still accountable for compliance and cannot assign liability for errors that result in fiscal sanctions for noncompliance to the contractor. The cost of this oversight, including the need for the district to continue to directly employ an administrator with signature authority for the program, should be weighed into the costs of the contract. Furthermore, it is important for the district to check the contractor's record for managing foodservice programs in other school districts.

Procurement

The responsibilities involved with following fair and competitive procurement procedures require careful consideration by school districts looking at outsourcing foodservice operations. The concerns are twofold: one, the procurement process for soliciting bids or requests for proposals (RFP) for the contract itself; and, two, the subsequent procurement of goods and services for the school foodservice program under the management contract.

Soliciting Foodservice Management Services

In regard to the solicitation process, federal rules exempt "small purchases" (USDA, 2003), which are defined as items less than \$100,000. If small purchases are used, the regulations require that "price or rate quotations shall be obtained from an adequate number of qualified sources." (USDA, 2003). All other purchases are subject to federal regulations found in 7 CFR § 3015, 3016 and 3019, which require full, fair, and open competition.

In 2004, the USDA published a set of proposed amendments to the federal regulations regarding procurement. The proposed amendments address issues raised by the 2002 OIG report, and they include extensive discussion of several areas of concern, including ethics, cooperative purchasing, and FSMC issues, as well as proposed changes to the regulations (Federal Register, 2004). The USDA evaluated those comments it received regarding the proposed regulation and drafted the final rule. For an explanation of the regulatory process, refer to "Government Relations" (Sackin, 2006). If a school district determines that contracting with a management company is in its best interest, the proposed rule requires that the contract either conforms to a prototype developed by the state agency responsible for child nutrition programs or includes language consistent with fair procurement as contained in the prototype contract. Furthermore,

all contracts and any material changes must be pre-approved by the state before they are executed.

The USDA does not find an FSMC or school district's failure to properly award a contract or incorporate changes, including review and approval by the state agency in a timely fashion, to be a compelling reason for undermining the procurement principles laid out in the proposed amendments. Under the recommended changes, such modifications would result in "unallowable" costs to the program, meaning that no federal reimbursement will be made to the district until it has complied with the law.

FSMC Procurements

The second area of concern is procurement by a contractor on behalf of the district in performing its duties under the contract. A frequently cited reason for seeking an FSMC to manage a foodservice program is their extensive buying power. Unfortunately, the 2002 USDA report found that, in many cases, the cost and benefits of these resources were not passed to the school district. The proposed amendment on procurement states:

"[The 2002 USDA report] revealed problems in several cost-reimbursable contracts between school food authorities and foodservice management companies. Some contracts between school food authorities and foodservice management companies lacked controls as to exactly how the company would determine the allowability of costs charged to the school food authority, including how the company would provide the school food authority with the benefits of purchase discounts and rebates in the determination of net costs." (Federal Register, 2004)

The school board is responsible for ensuring, through appropriate contract language and review, that the district has access to and can benefit from the FSMC's buying leverage. It is through the use of these resources that FSMCs are able to profit at the expense of the district and ensure low costs to the district. By retaining incentives, whether they are as a result of increased buying leverage or through special promotions offered by the vendor, the company is able to generate revenue for its procurement division or commissary. This contributes to the company's overall profits and may not accrue to its contract management operations.

Ensuring that districts benefit from FSMC procurements and verifying that utilization of such commodities are made available to school districts should be key concerns to any district considering an FSMC contract. According to the USDA report:

"Four of the five companies that operated under fixed-rate contracts at 46 SFAs we reviewed withheld credit for \$5.8 million in USDA-donated commodities that were used in the NSLP. The management companies profited by using the USDA-donated commodities and failing to properly credit those SFAs with the commodities' value" (USDA, 2002).

The proposed regulations point to areas that require especially vigilance by a school board in regard to the contracting and oversight of the foodservice program. The intent is to ensure that program funds are fully utilized for the benefit of program recipients.

It is possible for school districts to enjoy benefits similar to those achieved through the volume buying power of large corporations. The USDA's Commodity Order Re-Engineering (CORE) Team report, which summarized the results of teams assigned to evaluating the USDA commodity program, found that schools were advised that the agency should:

"Encourage and assist in the development of [purchasing] co-ops. Over the past several years, an increasing number of districts have joined together to increase [their] buying power. This has resulted in decreased costs and increased accessibility to processed items and distribution services." (USDA, 1999)

Marketing, Program Quality, and Nutrition Education

Federal law is designed to promote participation in the not-for-profit school meal program by restricting sales of food that compete with school meals. The regulations define competitive foods as "any foods sold in competition with the Program to children in foodservice areas during the lunch periods."(USDA, 2003) Under this definition, sales through cafeteria a la carte lines are considered competitive food items. A GAO report determined that schools that contracted with FSMCs lagged far behind self-operated programs in school meal participation by as much as 28% (Slomba et al., 1996).

Federal regulations allow two primary approaches to menu planning: 1) food-based systems in which menus are planned using specific portions of items from each food group (meat/meat alternate, breads/grains, fruits/vegetables, and milk); and 2) Nutrient Standard Menu Planning (NSMP), in which the amount and types of food offered is less important than the nutrient content of the whole meal. As NSMP does not require specific amounts of foods, menus planned under this approach are often less costly than food-based menus. Following the approval of NSMP in the regulations, USDA published a report that discovered that lunch costs in elementary schools were significantly lower using the NSMP approach than the food-based system (\$1.23 and \$1.36, respectively) (USDA, 1998).

Although the NSMP approach requires sophisticated software and nutrient databases, FSMCs have a greater ability to apply the NSMP as they can develop menus concurrently for the large number of schools that they manage. Distributing the salaries of dietitians and the costs of database management over multiple contracts reduces the administrative costs associated with NSMP and, as a result, management companies can reduce these costs. Of course, there are a number of vendors that offer software, databases, and technical support to make NSMP an available option to all districts willing to make the initial investment. The downside to having an FSMC plan menus for a diverse range of school districts from a corporate office is that such menus may not reflect the regional and local food preferences of students in the way that a local menu planner would take into account.

The major FSMCs all have developed a variety of marketing and education tools that they make available to client districts. These programs are frequently value-added and fees are charged for incorporating them into the local contract. However, there are a growing number of resources available to districts to help self-operated programs develop and implement marketing and educational strategies. Unlike most segments of the foodservice industry, school districts do not compete with each other for business. As such, many school nutrition professionals who develop

extraordinary marketing and education tools are willing to share their knowledge, experience, and materials with their peers in other districts.

In regard to program evaluation, there are a number of tools available for self-operated programs in districts to use. In 2003, the School Nutrition Association (SNA) revised its self-assessment tool, *Keys to Excellence*, which encourages school districts to look objectively at the elements of their foodservice programs to recognize areas in which improvements can be made. The online tool includes links to Internet resources designed and available to help the district implement the improvements identified by the assessment. Perhaps of even greater value to a district is the wide range of experts available for short-term interventions that can improve the foodservice program. SNA includes a listing of consultants in the "CN Marketplace" area of its website, www.schoolnutrition.org. Individuals and companies that provide school foodservice consulting services often offer the professional expertise of former SNA members. These companies can analyze school nutrition operations using tools like *Keys to Excellence*, evaluate plans of improvement based on their own experience, and work with local school teams to initiate changes.

Seeking Support for Self-Operation

A school foodservice program is a complex web of federal, state, and local laws and policies to which a district must conform. As noted previously, the accounting framework for school foodservice is different than the system required for the rest of the district. The range of technology tools available for school meal operations requires special knowledge and expertise. Included in the regulatory environment, but viewed as a separate field of knowledge, is nutrition and menu planning. Procurement, personnel, cooking, storage and serving equipment, food safety and health codes, and distribution are additional operational areas that are unique to school foodservice programs. Additionally, like commercial foodservice operations, successful operators employ sophisticated marketing tools to enhance their programs.

Larger school districts frequently create an organizational structure that utilizes the specialized expertise of its staff to manage different operational areas. Smaller districts may have a few individuals who have multiple skills. Regardless of the size of the district or foodservice staff, it may be helpful to have a fresh set of eyes unencumbered with institutional myopia, who can look objectively at the foodservice program and offer recommendations for improvements. This is true even for well-run, successful programs. It may be in a district's best interest to undertake an objective review before making the decision to outsource the program. Such a review might conclude that contracting its foodservice program *is* the best option, and the results of the assessment will be helpful to the district in determining exactly what it requires of an FSMC.

When evaluating a school district in response to an RFP for management of the foodservice program, a FSMC may use a team of program experts to review the current foodservice operation and assess what tools will be needed to improve program performance and ensure financial success. These evaluations take a holistic approach and recognize the relationships among a variety of factors. Although districts that desire to have similar program improvements but maintain control of their programs may not have the ability to conduct similar evaluations, there are resources available to help facilitate this process.

Finding an individual or group that can provide a comprehensive analysis of a foodservice program may seem as daunting as the process of finding an FSMC to take over operations. There are a number of independent consulting groups that feature experts who possess a broad spectrum of experience to help districts improve their operations. The RFP process lends itself to being applied in finding an outside consultant to evaluate a program prior to requesting proposals from FSMCs or to help improve self-op programs. It may be that district administrators do not even know what questions to ask. The RFP process allows districts to establish a set of desired outcomes without limiting responses from companies. As a result, the very proposals that come in may help define the scope of work, as the district gains insight into the range of services and programs that can be offered.

In 2002, Florida's Orange County Public Schools (OCPS) system, one of the nation's largest school districts, issued an RFP to help improve its operations. The RFP read:

"The School Board has determined that it is seeking a Consultant to provide a management review of the District Business Plan for Food Service, and provide recommendations, technical assistance and training for the Food Service Department" (Orange County, 2002).

Under the scope of services, the RFP stated:

"The purpose of the project is to obtain a review of the District's Business Plan to reduce food costs, and provide recommendations to guarantee delivery of good service and provide a profit for the enterprise, technical assistance and training for the Food Service Department." (Orange County, 2002)

The RFP went on to provide additional processes for review and recommendation. This approach gave the district the broadest possible opportunity to receive creative solutions to its concerns. It was able to select a consulting group that had the resources to fully evaluate the program and present possible opportunities for improvement, as well as work with district staff to implement its recommended changes. In turn, this allowed OCPS to improve upon an already successful program, maintain full operational control of the program, and retain all of the revenue generated by the program to reinvest. As OCPS is a public entity, other districts may use the RFP it developed as a template for their own needs.

There are reasons why a school board may opt to outsource its foodservice program; however, the district needs to be fully aware that it remains responsible for the program. There are many mitigating factors found in the law that merit strong consideration by the district when implementing a contracting process. Finally, a school board must commit to treating its school foodservice program as an integral part of the educational environment. The shared goal of all the partners involved is the achievement of children, and the school should provide the best opportunity for them to succeed. Part of that goal is to ensure that children are healthy, well-nourished, and able to take advantage of educational opportunities offered to them in the classroom and beyond.

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BIOGRAPHY

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