



United States
Department of
Agriculture

Food and
Nutrition
Service

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DATE:

POLICY NO.: FD-007: Processing (Revised)

SUBJECT: Sales of End Products through Commercial Distributors
Indirect Discount and Net Off Invoice

The purpose of this policy memorandum is to clarify requirements in the sale of processed end products through a commercial distributor under an “indirect discount” or “hybrid” sales system, in accordance with 7 CFR 250.30(e)(1)(ii), and in a modified form of such sales system previously approved by the Food and Nutrition Service (FNS), in accordance with 7 CFR 250.30(e)(1)(iii). This policy memorandum revises the previous FD-007, which was dated March 18, 2003.

Indirect Discount and Net Off Invoice

In accordance with 7 CFR 250.30(e)(1)(ii), under indirect discount sales, a distributor sells end products received from processors to school food authorities (SFAs) or other recipient agencies at a discount from the gross commercial case price, to account for the value of the donated foods contained in or used to produce the end products. The distributor must subsequently submit an application for a refund or rebate to the processor in order to receive compensation for the discount provided to the SFA.

In order to streamline this process, FNS approved a variation of this system, called “Net Off Invoice” (NOI), that permits a distributor to request, or receive, such compensation through its electronic sales velocity reports, or other automated sales reports, which also serve to notify the processor of end product sales. Once such sales reports are received, the processor can report end product sales and inventory reductions of donated foods to the State distributing agency (SDA) in its monthly performance reports. The processor and the distributor must work out the logistics of compensating the distributor for the donated food value.

Processed end products can only be sold at a discount if the processor has an approved end product data schedule and the end product has been approved by the SDA. Before a processor is allowed to draw down inventory, it must verify that the customer is an eligible recipient agency.

Ensuring Sales of End Products to Eligible SFAs

The processor and distributor should collaborate closely to ensure that end products are sold only to SFAs eligible to receive them, and that such end products are sold in a timely manner. To this end, the processor must provide the distributor with a list of SFAs eligible to receive end products, and either:

- 1) The quantities of approved end products that each SFA is eligible to receive (cases or dollars); or
- 2) The quantity of donated food allocated to each SFA, and the raw donated food (pounds or dollars) approved per case of end product.

Commingling of Finished End Products and Commercial Products

The processor must inform the distributor that processed end products may be commingled with commercial products that are identical to such end products (i.e., meet substitution requirements in 7 CFR 250.30(f) and grading requirements in 7 CFR 250.30(g)) at the distributor's facility. The distributor may sell such commingled commercial products and finished end products to any of its customers, but must sell them to eligible SFAs with a discount for the value of the donated food.

For end products produced from non-substitutable donated foods, the processor must assign end products a unique shop keeping unit (SKU) or other identifier to prevent commingling or slotting with similar commercial products, which do not meet USDA's specification, substitution, and grading requirements, at the distributor's facility. These closed SKU non-substitutable end products must only be sold to eligible SFAs. The processor must also provide the distributor with the gross price of the end product, and the value of the donated food used to produce the end product for each SKU. The processor should also notify SFAs that end products have shipped to the distributor, so that they can begin drawing down the inventory.

The distributor may use an indirect discount or NOI system to provide notification of end product sales to the processors, if such system has been approved by the SDA and the processor.

Verification of Sales

The information in this section clarifies requirements for sales verification for processors that deliver end products made with donated foods through commercial distribution channels, and that elect to meet requirements through NOI or other electronic methods.

Several private companies have developed electronic systems for tracking SDA and SFA inventory at processors, and managing distributors' sales velocity report data and sales verification. Such systems must, at a minimum, include a component that documents that an

SFA has accessed account information that would allow for validation that the appropriate value of donated food was received from the commercial distributor. At a minimum, documentation for electronic sales verification must include a user account access identifier (user ID or email address), the name of the processor(s) and the date/time of access.

Alternatively, the SDA may require SFAs to verify receipt of end products and the appropriate donated food value through email communication. The SDA may also choose to accept a "read receipt" of an email message sent to the SFA as confirmation that the SFA has accessed or reviewed processor account information to determine if the appropriate value of donated food was provided by the commercial distributor. An SFA choosing not to respond to such email message would be positive verification that the information contained in the message is correct. This procedure may also be used by SDAs that use email to re-verify the processor's sales verification, in accordance with 7 CFR 250.19(b)(2)(vi)(C). As further assurance that it receives the requisite value of donated foods in end products, the SFA should indicate that a bid submitted in response to its solicitation for procurement of end products must include the gross case price, the donated food value, and the net case price.

The use of indirect discount or NOI as a mechanism for passing the value of donated food is not mandatory, and SDAs may choose to disallow such means of value pass-through. Please direct any questions regarding this policy memorandum to David Brothers at (703) 305-2668 or Sherry Thackeray at (703) 305-2652.



Laura Castro

Director

Food Distribution Division