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**Via Email and U.S. Mail**

The Honorable Claire McCaskill  
Senate Committee on Homeland Security & Governmental Affairs  
Ad Hoc Subcommittee on Contracting Oversight  
Hart Senate Office Building, Ste. 506  
Washington, D.C. 20510

Re: Post-Hearing Questions for the Record Submitted  
to Assistant Attorney General John F. Carroll, Jr.

Dear Senator McCaskill:

Please accept New York Attorney General Eric T. Schneiderman's greetings and thanks for your continued concern regarding the National School Lunch Program (NSLP) and off-invoice rebating. Below you will find answers to the subcommittee's Post-Hearing Questions forwarded to me on October 5, 2011.

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1. *What role do the suppliers and other companies who pay the rebates play in these schemes?*

A: (1) Suppliers, and distributors (collectively, vendors) enter into agreements with Food Service Management Companies (FSMCs) for vendors to pay FSMCs off-invoice rebates in situations where the vendors are aware that the products are destined for NSLP or government clients; (2) vendors are aware of United States Department of Agriculture (USDA) regulations and other government contracting regulations; (3) vendors appear to have an interest in a lack of transparency; and (4) to the extent rebates are re-characterized as anything other than what they are, vendors participate in this change in nomenclature.

2. *Many food service management companies use their own in-house food distributors. Should this make us more or less cautious in our oversight of their rebate practices?*

A: The practice lessens transparency. Though this would not necessarily be determinative of questionable rebate practices, FSMC business activities which increase the complexity of the "bean counting" of rebates, can undermine the Government's interest in receiving its full share of rebate payments. A recent investigation and prosecution by the U.S. Department of Justice discussed at the hearing provides strong reason to believe that interposing corporate entities in the stream from vendor to NSLP or other government purchaser will, at a minimum, increase opacity and, at worst, may constitute a fraudulent effort to conceal.

3. *Did you contact the Department of Justice about your investigation?*

A: The original Sodexo investigation was triggered by a *qui tam* action filed in the United States District Court for the District of Massachusetts by the firm of Phillips and Cohen, in which U.S. government entities were named as parties. As such, the United States and the U.S. Department of Justice (DOJ) were aware of the allegations from inception of the *qui tam* matter.

The Office of the New York Attorney General has publicly announced its rebate investigation and settlements, and those announcements have been covered in the media.

4. *Did the Department of Justice provide a reason as to why it chose not to intervene in the case?*

A: Consistent with DOJ policy, OAG was not formally informed of the DOJ's reasons for declining to intervene in the *qui tam* action.

5. *I have also learned of a practice called "silo-ing," where the contractors buy food for all their clients and amass rebates based on the overall volume of purchases, but because all of the product is "silo-ed" together, the contractor can't allocate the rebates to individual clients. Is this a credible commercial practice?*

A: Interposing silo-ing as the sole basis to avoid crediting rebates to clients is a questionable justification since the sum of rebates can be readily divided mathematically and *pro rata*.

6. *In your opinion, what are some of the biggest challenges for schools to effectively manage and oversee these contracts?*

A: The single main challenge is the fact that rebates are paid directly to FSMCs by vendors without specific knowledge of clients. Correspondingly, our investigation has found that when clients ask their FSMCs about rebates, FSMCs do not clearly and consistently articulate amounts or bases for the rebate payments, making it exceedingly difficult for clients to police their own agreements.

7. *Dating as far back as 1969, the Food and Nutrition Service (FNS) has issued guidance and prototypes for use by school districts when entering into agreements with Food Service Management Corporations, and has continually addressed this issue in the 4 decades since. In 2007, FNS provided explicit instructions to local schools regarding appropriate contractual provisions to ensure savings are passed on by the contractor. In your view, is there anything unclear about the guidance provided by FNS?*

A: In my view, the rule is clear and is also consistent with Generally Accepted Accounting Principles which provide that cost representations must be net of discounts and rebates.

As noted in response to Question 6, the main obstacle to enforcement is the inherent lack of transparency to rebating.

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To close, Attorney General Schneiderman looks forward to continuing to support the sub-committee's efforts. Should you wish to contact our office further in connection with your investigation, please contact Randall Fox at 212-416-6199. Thank you once again for your time and attention to this important issue.

Respectfully submitted,



John F. Carroll  
Assistant Attorney General