



Houston Independent School District Internal Audit Report: Nutrition Services Department

February 26, 2024



TABLE OF CONTENTS

Transmittal Letter	1
Executive Summary	2
Background.....	6
Objectives and Approach	14
Observations Matrix	15
Appendix A – Flow Charts	22



TRANSMITTAL LETTER



February 26, 2024

The Audit Committee of
Houston Independent School District
4400 W 18th St.
Houston, Texas 77092

Pursuant to the approved internal audit plan for fiscal year ("FY") 2023-2024 for Houston Independent School District ("HISD"), we hereby submit the internal audit of the Nutrition Services Department ("NSD"). This internal audit focused on the NSD's inventory receiving, cash safeguarding, invoice processing, and fixed asset verification processes. We will present this report during the Audit Committee meeting scheduled for April 16, 2024.

Our report is organized into the following sections:

Executive Summary	This provides a high-level overview and summary of the observations noted in our internal audit of the Nutrition Services Department.
Background	This provides an overview of the function and relevant background information.
Objectives and Approach	The internal audit objectives are expanded upon in this section, as well as a review of the various phases of our approach.
Observations Matrix	This section includes a description of the observations noted during our internal audit and recommended actions, as well as Management's response, including the responsible party, and estimated completion date.
Appendices	This section provides additional information, including a visual depiction of the workflow of key processes.

We would like to thank the staff and all those involved in assisting our firm with this internal audit.

Respectfully Submitted,

RSM US LLP

Internal Audit



EXECUTIVE SUMMARY

Houston Independent School District – NSD

Nutrition Services Overview



Mission & Vision

The Nutrition Services Department (NSD) provides school meal programs to ~274 school cafeterias and satellite locations within the District. Their mission is to provide students with high-quality nutritious meals, impeccably served, while inspiring the development of dietary habits that enhance academic performance and lifelong health. Their vision is to be recognized as the greatest urban school district food service program in the nation.

FY 2023 Annual Comprehensive Financial Report Highlights

\$55M	Starting Fund Balance	
\$145M	Actual Revenue	
\$128M	Actual Expenditures	
\$72M	Ending Fund Balance	
Revenues since FY 2019	Expenditures since FY 2019	Ending Fund Balance since FY 2019
+9%	-2%	2.4x

FY 2023 Top Spend by Category

Supplies and Materials	\$71.7M
Payroll Expenses	\$49.4M
Other Operating Expenses	\$8.5M

FY 2023 Top Spend by Vendor

Labatt Inst. Supply	\$41M
Hardie's Fruit and Vegetables	\$9.4M
DFA Dairy Brands	\$8M
Kurz & Co.	\$1.9M
Brandt Constructors	\$0.6M

Internal Audit Objectives

The objective of this internal audit was to assess the design and operating effectiveness of controls within HISD NSD. This internal audit focused on the NSD's inventory receiving, cash safeguarding, invoice processing, and fixed asset verification processes to identify opportunities for improvement and enhance compliance with relevant laws and regulations, if applicable.

Our approach included the following procedures:

- Conducted interviews and walkthroughs to understand District policies, procedures, and responsibilities.
- Developed a plan to assess control effectiveness and process efficiency.
- Evaluated NSD policies and procedures for adequacy and access.
- Reviewed control structures for policy compliance.
- Analyzed inventory receipt and documentation adequacy.
- Evaluated employee training processes.
- Examined the review procedures for outsourced services and related contracts.
- Examined inventory procurement for non-standard activities.

At the conclusion of this internal audit, we summarized our findings into this report. We have reviewed the results with the appropriate Management personnel and have incorporated Management's responses into this report.



EXECUTIVE SUMMARY (CONTINUED)

Observation Summary

Provided below are the observation risk rating definitions for the detailed observations.

Observation Risk Rating Definitions	
Rating	Definition
Low	Observation presents a low risk (i.e., impact on financial statements, internal control environment, or business operations) to the organization for the topic reviewed and/or is of low importance to business success/achievement of goals. Action should be taken within 12 months (if related to external financial reporting, must mitigate financial risk within two months unless otherwise agreed upon).
Moderate	Observation presents a moderate risk (i.e., impact on financial statements, internal control environment, or business operations) to the organization for the topic reviewed and/or is of moderate importance to business success/achievement of goals. Action should be taken within nine months (if related to external financial reporting, must mitigate financial risk within two months).
High	Observation presents a high risk (i.e., impact on financial statements, internal control environment, or business operations) to the organization for the topic reviewed and/or is of high importance to business success/achievement of goals. Action should be taken immediately, but in no case should implementation exceed six months (if related to external financial reporting, must mitigate financial risk within two months).



EXECUTIVE SUMMARY (CONTINUED)

Observation Summary

Below is a summary of the observations identified during this internal audit. The observation matrix includes detailed observations.

Summary of Observations	
Observations	Rating
<p>1. Inventory Management: Hazardous Cleaning Supplies</p> <p>Condition: Improper storage of hazardous cleaning supplies was observed at one site, and there was a lack of clear separation from food storage/preparation areas, posing contamination risks.</p> <p>Recommendation: Consider re-emphasizing cleaning supply storage expectations and enhancing current required employee training on handling, storage, and use of hazardous cleaning supplies. This training should also be part of new employee onboarding orientation.</p>	High
<p>2. Inadequate Fixed Asset Verification</p> <p>Condition: Fixed asset verification was not conducted in FY 2023. 54 assets reviewed lacked sufficient documentation for accurate asset management.</p> <p>Recommendation: Consider assigning a dedicated NSD employee to manage and validate the accuracy of the fixed asset verification process, with results communicated to the Fixed Asset Department for action. The Fixed Assets Managers should conduct training for NSD Leadership on guidelines and procedures for effective fixed asset verification.</p>	High
<p>3. Inadequate Cash Safeguarding</p> <p>Condition: Unlocked safe boxes containing cash were found at two locations, indicating lapses in safeguarding cash.</p> <p>Recommendation: Consider reinforcing the importance of secure cash storage by updating and distributing specific guidelines on safe box access and locking procedures. Initiate training for Team Leads and staff to promote strict compliance with cash handling protocols.</p>	Moderate
<p>4. Inventory Management: Inconsistent Order Discrepancy Process</p> <p>Condition: Inadequate documentation and communication of discrepancies in received goods were observed at 5 of 8 sites.</p> <p>Recommendation: Consider training Team Leads on guidelines, procedures, and resources to reconcile invoices, orders, and receipts in Primero accurately. Develop a consistent process for documenting discrepancies and returns in the "Outside Vendor Discrepancy & Credit/Return Spreadsheet," especially when received items differ from the invoice.</p>	Low
<p>5. Inventory Management: Deviation from First-In-First-Out (FIFO) Procedures</p> <p>Condition: Deviation from the FIFO method due to freezer space constraints at one site.</p> <p>Recommendation: Consider offering training for Team Leads and kitchen staff on using the FIFO method for accurate inventory management and waste reduction, including procedures for handling exceptional inventory situations. Improve inventory monitoring to reduce duplications, optimize freezer space, and assess the need for extra deliveries at specific locations based on storage and business requirements.</p>	Low



EXECUTIVE SUMMARY (CONTINUED)

Observation Summary (Continued)

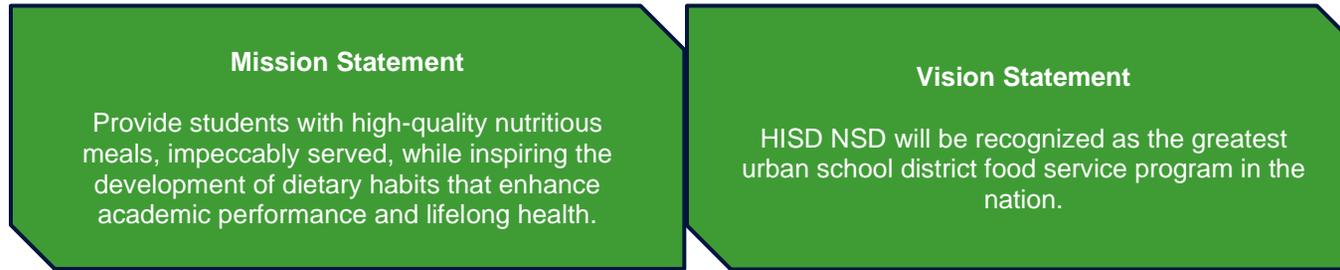
Summary of Observations	
Observations	Rating
<p>6. Inventory Management: Inconsistent Food Temperature Practices</p> <p>Condition: Inconsistencies in temperature verification of delivered frozen and refrigerated items were observed, risking food safety and compliance with procedural requirements.</p> <p>Recommendation: Train kitchen staff on proper storage practices to prevent the use of spoiled inventory and maintain food safety. Operations Coordinators should enforce food safety standards in their zones, including immediate temperature checks for frozen and refrigerated items before storage, to enhance food safety and optimize storage conditions for perishables.</p>	Low
<p>7. Bennington Warehouse Facility:</p> <p>Condition: The warehouse is underutilized with significant annual costs, presenting opportunities for improved utilization or alternative options.</p> <p>Recommendation: Considering conducting a cost-benefit analysis of the Bennington Warehouse to assess the economic impact of its current and potential uses, such as repurposing or selling the property and equipment. The results should inform strategic decisions to optimize resource allocation for NSD's goals and enhance District efficiency.</p>	Low



BACKGROUND

Overview

The Nutrition Services Department (“NSD”) provides school meal programs to ~274 school cafeterias and satellite locations within the District. The NSD’s primary functions include procuring food, meal planning, preparation, and distribution in accordance with federal and state nutritional standards. The NSD provides breakfast, lunch, snacks, and dinner services and serves over 193,000 meals daily¹.



Organizational Structure

The NSD employs approximately ~1,400 employees across four (4) subdivisions.



¹ Page 34 of the FY 2023 Adopted Budget Book



BACKGROUND (CONTINUED)

Financial Overview

The NSD’s financial operations are grounded in federal and state program participation, including the School Breakfast Program and National School Lunch Program. These programs offer partial cost reimbursement for qualifying meals. The balance of meal service costs is managed through cash sales from a la carte items, staff and visitor meals, and state-matching funds. HISD schools benefit from the Community Eligibility Provision, which provides free meals to students. Additionally, the NSD participates in several other federal and state nutrition initiatives to enhance student access to nutritious foods.

Revenues

Total revenue has increased 9% from FY 2019 to FY 2023. The NSD’s revenues are primarily derived from the United States Department of Agriculture (“USDA”) through the National School Lunch Program. Over 80% of HISD students are eligible for free or reduced-price meals through this program. See *Figures 1* and *2* below for NSD revenue over the past five (5) years, according to the FY 2019 – 2023 Annual Comprehensive Financial Reports (“ACFR”), the FY 2024 Budgeted revenue, and the FY 2024 actuals as of January 31, 2024.

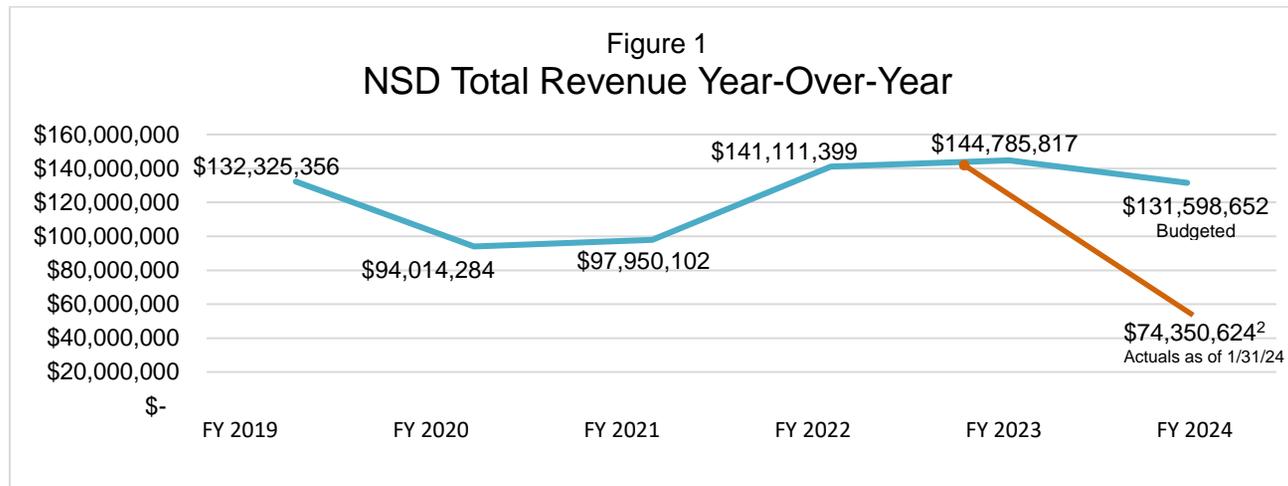


Figure 2 - NSD Revenues by GL Category

Categories:	FY 2023	YTD FY 2024 ²
Food Sales	\$ 5,123,442	\$ 2,790,097
Nutrition Programs	\$126,827,637	\$ 63,853,599
Donated Commodities	\$ 9,080,550	\$ 5,601,763
Interest Income	\$ 3,167,822	\$ 2,101,892
Misc. Revenues	-	\$ 3,273
Grand Total:	\$144,785,817	\$74,350,624

² Actuals are from 7/21/2023 to 1/31/2024

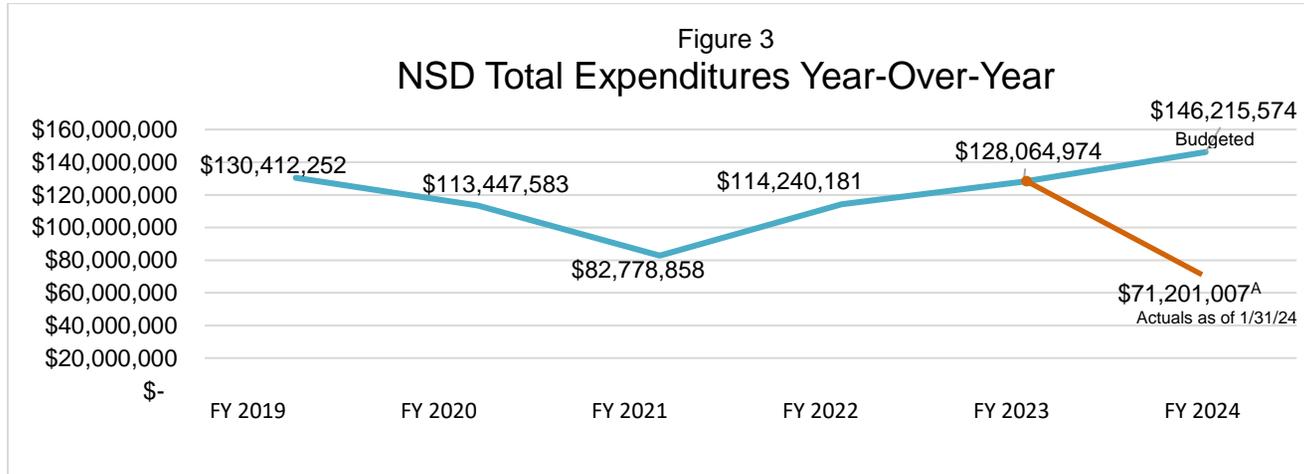


BACKGROUND (CONTINUED)

Financial Overview (continued)

Expenditures

As of FY 2023, total expenditures have decreased 2% since FY 2019. In FY 2023, NSD budgeted expenditures accounted for 3.77% of all budgeted expenditures throughout the District. See *Figure 3* below for NSD expenditures over the past five (5) years, according to the FY 2019 – 2023 ACFRs, the FY 2024 Budgeted expenditures, and the FY 2024 actuals as of January 31, 2024.



Please refer to *Figure 4* below for NSD expenditures by GL Category for FY 2023 and the actual Year-to-Date (YTD) for FY 2024 as reported by Nutrition Services Compliance & Accountability. Please refer to *Figure 5* below for the top 10 NSD vendor spending for FY 2023.

Figure 4 - NSD Expenditures by GL Category		
Categories:	FY 2023	FY 2024 ²
Supplies and Materials	\$ 71,709,856	\$ 47,945,996
Payroll Expenses	\$ 49,398,873	\$ 12,945,740
Other Operating Expenses and Indirect Costs	\$ 1,504,438	\$ 5,325,856
Professional and Contracted Services	\$ 4,804,031	\$ 3,837,638
Capital Outlay	\$ 375,518	\$ 1,145,777
Debt Service	\$ 272,257	-
Grand Total:	\$ 128,064,974	\$ 71,201,007

Figure 5 - Spend by Top 10 Vendors FY 2023	
Labatt Institutional Supply Company	\$ 41,001,273
Hardie's Fruit and Vegetables Co.	\$ 9,367,070
Dfa Dairy Brands Corporate, LLC	\$ 7,974,740
Kurz & Co.	\$ 1,859,239
Brandt Constructors & Facility Serv	\$ 584,431
Southwest Disposal, L.L.C.	\$ 399,890
Sysco USA I, Inc	\$ 371,122
Paleteria El Pibe, Inc.	\$ 322,683
United Refrigeration Inc.	\$ 283,673
Cybersoft Technologies Inc	\$ 272,257

² Actuals are from 7/21/2023 to 1/31/2024.



BACKGROUND (CONTINUED)

Operations

The NSD operates under regulatory guidelines set forth by the USDA and the Texas Department of Agriculture.

The NSD manages the largest school nutrition program in Texas and thus navigates multiple operational challenges. The NSD must coordinate meal services based on various school schedules, and staff turnover and labor force shortages are common within the NSD. NSD departments in all districts encounter food distribution supply chain challenges, including transportation delays, perishability issues, complexities in inventory management, fluctuations in demand, adherence to regulatory requirements, and the imperative of upholding stringent quality standards across the entire supply chain. Furthermore, the emergence of external food delivery services requires the NSD to position its meal programs to remain competitive strategically. Adapting to changing food trends and student dietary preferences is a continuous effort to maintain its meal offerings' nutritional quality and attractiveness.

To address these challenges, the NSD consulted a third-party firm specialized in warehousing and distribution services to conduct a cost-benefit analysis in May 2020. The analysis compared the NSD's expenses, including labor, utilities, and other costs, against the costs of a comparable school district. The analysis revealed that the NSD could reduce total costs by approximately \$2-4 million annually while avoiding anticipated capital expenditures of approximately \$5 million in the following 2-4 years for truck and refrigeration system replacements. Following the analysis, the NSD underwent structural changes, transitioning from a central warehouse to a decentralized model (the "Broadline Distribution model") managed by an external supplier, Labatt Institutional Supply Company, which commenced operations in July 2021. The Broadline Distribution model utilizes just-in-time inventory instead of centralized warehousing, enhancing flexibility. In this operational framework, individual schools are responsible for initiating orders and prompting the distributor to deliver the food and goods to each kitchen. The Nutrition Services personnel at the schools then prepare, cook, and serve the meals to the students. The objective of the Broadline Distribution model is to be cost-effective, promote consistent quality, and enhance risk mitigation. The supplier is responsible for food safety protocols, reducing the risk of foodborne illnesses and non-compliance with health and safety standards.

Policies and Procedures / Employee Training

NSD has established policies, procedures, and training programs to define and enforce compliance and operational efficiency across varying staff roles. These guidelines cover essential operational aspects, including uniform standards, safety protocols, and performance evaluations. New employees undergo a structured two-day orientation, with the first day dedicated to general employment practices and the second to specialized training in kitchen operations, such as safe food handling and adherence to state regulations. Regular and annual training sessions are conducted to facilitate professional development and compliance with national standards.

The Operations Coordinators, with the assistance of on-site Team Leads, oversees the training compliance. Standard Operating Procedures (SOPs) for goods receiving and inventory management are regularly reviewed and updated to align with best practices and regulatory requirements, supporting the department's commitment to operational excellence and safety in food handling. These SOPs are integral to NSD's efforts to promote health and safety, guiding the process for the receipt of food items in a manner that aligns with established guidelines.



BACKGROUND (CONTINUED)

Operations (Continued)

Inventory Receipt

The inventory receipt process is designed to adhere to the compliance standards and guidelines of the USDA and the Texas Department of Agriculture. Each school has a designated Food Services Attendant Team Lead (“Team Lead”) that oversees this process. Receipting begins when the Team Lead receives a hard copy of the invoice and goods from the delivery driver. The process involves the following³:

1. **Quality Inspection:** The Team Lead conducts a thorough inspection to identify any visibly damaged goods and record the temperature of delivered items.
2. **Quantity Verification:** The Team Lead validates the delivered quantity matches the invoice details.
3. **Documentation:** The Team Lead and the delivery driver sign the invoice, with the delivery date noted on the inventory packaging.
4. **Storage:** The Team Lead and general kitchen staff utilize the First-in-First-out (“FIFO”) method to store received goods, arranging inventory with older items positioned towards the back in freezers, refrigerators, and pantries.
5. **System Entry:** The Team Lead completes the goods receipt transaction in PrimeroEdge, verifying the receipt of ordered items against the order and documenting any discrepancies or substitutions.
6. **Discrepancy Reporting:** The Team Lead records any discrepancies in the shipment on the Discrepancy Form and forwards it to either the customer service department or the Operations Coordinator for a thorough review.
7. **Damage Reporting:** The Team Lead completes the documentation of shipment discrepancies on the Discrepancy Form and subsequently sends the form to the customer service department or Operations Coordinator for review.

Invoice Processing

Invoice processing is handled by a team of seven employees within the HISD Accounts Payable (“AP”) department, who are assigned to support the NSD. The process involves the following³:

1. **Initial Data Capture:** Upon invoice receipt, Optical Character Recognition technology extracts key information such as quantity, unit price, vendor information, total price, purchase order number, and applicable taxes from the invoice, and the invoice details are systematically input into SAP.
2. **Invoice Matching:** The AP Analyst assesses the Vendor Invoice Management (VIM) Workplace inbox within SAP and matches the invoice with the corresponding purchase order (“POs”) and goods receipt (“GR”) in SAP to complete the three-way match.
3. **Discrepancy Resolution:** When there is a discrepancy between the invoice, GR, or PO, the AP Analyst contacts the applicable department or vendor through email to identify and address the root cause of the discrepancy. Upon successful resolution, the AP Analyst routes the invoice to batch processing within SAP.
4. **Non-PO Invoice Processing:** When an invoice without a corresponding PO is received, The AP Analyst routes the invoice and any other supporting documentation within SAP to the appropriate department for approval. Once the invoice is approved within SAP, the AP Analyst routes it to batch invoice processing within SAP.
5. **Service (No Goods Receipt) Invoice Processing for Concession Vendors:** When an invoice related to a service (no physical goods receipt) is received, the AP Analyst creates a shopping cart within SAP acting as a goods receipt for the transaction. Once the shopping cart is created, the AP Analyst routes the invoice to batch processing within SAP. The Concession Vendor is a vendor that has a preauthorized concession agreement with HISD.
6. **Batch Payment Approval:** Upon successfully matching the invoice with the GR or PO or obtaining the necessary approval, the invoices are consolidated into an invoice batch within SAP. Subsequently, the AP Manager authorizes the invoice batch for payment processing.

³ Reference *Appendix A* for detailed flowcharts related to Inventory Receipt



BACKGROUND (CONTINUED)

Operations (Continued)

Facility Maintenance

HISD has two (2) primary facilities maintenance teams: the District's Facility Maintenance Operations ("FMO") team, which is dedicated to general facilities maintenance for all HISD, and the NSD Facilities Maintenance team, which is solely responsible for NSD-owned equipment. The FMO promotes the optimal functioning, safety, and upkeep of the District's physical infrastructure, including buildings and equipment outside the school kitchens. Conversely, the dedicated NSD Facilities Maintenance team for the NSD focuses solely on equipment used for kitchen operations. Both departments share similar operations, conducting routine maintenance tasks, responding promptly to emergency repairs, managing assets, and maintaining accurate records of maintenance activities. The Team Lead from the schools contacts the facilities maintenance team dedicated to the NSD via phone to initiate a work order, which is documented and given a priority ranking by the Facilities Maintenance team. Simultaneously, the Team Lead records the work order in an internal log to track the completion timeline. Depending on priority, the facilities maintenance team performs the necessary work to satisfy the requirements outlined in the work order.

Fixed Asset Management

The Fixed Asset Department ("FAD") focuses on maintaining accurate records through an annual fixed asset verification process. Annually, the FAD generates the fixed asset ledger from SAP for all HISD departments and categorizes assets by SAP plant number. Once separated, the FAD distributes the fixed asset ledger to the respective department head. Specifically, for the NSD, the department head distributes the fixed asset ledger to the respective employees within the department to conduct verification procedures, including a detailed inspection of kitchen equipment, vehicles, and other tangible assets, validating their presence and that their condition matches the recorded details. The NSD employee conducting the count will note discrepancies between the fixed asset ledger and the fixed assets that were physically present. Inventory count results are provided to the FAD so that the master fixed asset ledger can be updated.



BACKGROUND (CONTINUED)

Operations (Continued)

Hexser T. Holliday Food Services Support Facility

The Hexser T. Holliday Food Services Support Facility (“Bennington Warehouse”), located at 6801 Bennington St, Houston, TX 77028, was previously central to the NSD in-house food production and operations. As of July 2021, it has been repurposed, as noted on page 8. Refer to *Observation #7 for additional details and RSM’s recommendation.*

Key highlights related to the building include:

- 219,000 square-foot facility, located on 15 acres.
 - 198,000 square feet on the first floor, 21,000 square feet on the second floor, and a 33-bay dock.
 - Facilities within the warehouse include a production area, a refrigeration system, a cooler, office space, a training room, a computer lab, and substantial dry storage space.
- Currently, the warehouse serves multiple functions:
 - Upstairs and Downstairs: ~150 NSD administrative, maintenance, and operations employees utilize office space.
 - Downstairs: HISD IT Department stores IT equipment within the large walk-in refrigerated area.
 - Downstairs: NSD’s catering business, Houston Eats, currently utilizes the kitchen and cooler to perform its operations. See page 12 for additional information.
 - Downstairs: Training room with a 150-person capacity is used for NSD staff on-boarding twice a month, as well as various other NSD and Business Operations conferences, trainings, etc.
 - Downstairs: Computer lab for NSD employees to complete compliance and other required training as needed.
 - Downstairs: Various NSD maintenance equipment is stored.
 - Parking Lot: NSD fleet of 140 vehicles for Operations Coordinators, QC, IT, FAL, Catering and Maintenance staff are stored.

Based on inquiry and on-site visit, the following capacity estimates were calculated related to the Bennington Warehouse:

- First Floor: 198,000 square feet with 80% vacancy. Therefore, 158,400 square feet are underutilized or unnecessary based on current usage.
- Second Floor: 21,000 square feet of office space with no vacancy; the staff fully utilizes NSD space.

The total Bennington Warehouse expenses for FY 2023 amounted to \$4,4348,980. The top nine expense categories for Bennington Warehouse in FY 2023 are shown in *Figure 6.*⁴

Figure 6 Top 9 Bennington Expenses FY 2023			
Property Insurance	\$ 936,386	Xtr Pay/OT-Sup Sal	\$ 269,931
Electricity	\$ 408,673	Hourly Pay	\$ 226,473
General Supplies	\$ 371,268	Purch. Food-Charges	\$ 211,899
Misc. Contract Services	\$ 299,174	Contracted Maintenance	\$ 205,802
SBITA Principal	\$ 271,407		

⁴ Expense detail was provided by the Executive Director of Compliance & Accountability utilizing data from SAP for Fund 2400010000 for the following SAP Cost Centers: 1040830000, 104083100, 1040833000, 1040836000, 1040836000, 1040837000, 1040838000, 1050806060.



BACKGROUND (CONTINUED)

Operations (Continued)

NSD Catering – Houston Eats

Houston Eats, situated within the Bennington Warehouse, is the NSD’s proprietary catering service initiated in 2004. Houston Eats provides meals for HISD meetings, dinner parties, conferences, and luncheons. Initially serving 250,000 meals monthly with a workforce comprising 23 drivers and 70 staff, the service has adapted to evolving District requirements and presently operates with an 18-member team with year-round service. Notably, the team adheres to predefined work schedules, with some overtime primarily incurred for late events. Additional fees for their services are collected for out-of-hours operations to provide structured management and financial sustainability within the catering line of business.

Reference *Figure 7* for details related to Houston Eats revenue and expenses for FY 2023. ⁵

Figure 7 Catering Revenue and Expenses FY 2023 ⁶		
Revenue Total		\$201,973
Expenses		
Purch. Food-Charges/Food Transfer Net	\$77,460	
Non-Food Supplies	\$44,014	
Xtr Pay/OT-Sup Salary	\$23,893	
Hourly Pay	\$14,450	
General Supplies	\$1,761	
Xtr Pay/OT-Supp Hourly	\$1,419	
Contracted Maintenance	\$200	
Expense Total		\$163,197
Total Profit		\$38,776

⁵ Catering Revenue and Expense detail was provided by the Executive Director of Compliance & Accountability utilizing data from SAP for Fund 2400010000 for the following SAP Cost Center 1040840000.

⁶ Immaterial differences in totals may be present due to rounding.



OBJECTIVES AND APPROACH

Objectives

The objective of this internal audit was to assess the design and operating effectiveness of controls within HISD NSD. This internal audit focused on the NSD's inventory receiving, cash safeguarding, invoice processing, and fixed asset verification processes to identify opportunities for improvement and enhance compliance with relevant laws and regulations, if applicable.

Approach

Our approach consisted of the following phases:

Understanding and Documentation of the Process

This phase consisted primarily of inquiry and walkthroughs to obtain an understanding of the current operating policies and procedures, monitoring functions, and control structures as they relate to the processes within our scope. The following was performed as part of this phase:

- Obtained and reviewed policies and procedures related to the in-scope areas and relevant information.
- Conducted interviews and walkthroughs with key personnel to obtain a detailed understanding of relevant operating policies and procedures, roles, and responsibilities within NSD.
- Gained an understanding of procedures related to the processes within scope.
- Developed a work plan to evaluate the operating effectiveness of procedures and controls based on the information obtained through interviews, walkthroughs, and preliminary documentation review.

Evaluation of the Process and Controls Design and Testing of Operating Effectiveness

The purpose of this phase was to evaluate the design of key processes and controls and test compliance and internal controls for operating effectiveness based on our understanding of the processes obtained during the first phase. We utilized sampling and other internal auditing techniques to meet our objectives outlined above. Our testing procedures included, but were not limited to:

- Performed site visits at 8 locations to assess inventory management procedures, verification of equipment condition, and cash safeguarding, including:
 - Verified the completion of a quality inspection for inventory receipt, validating proper rejection of damaged goods;
 - Confirmed the accuracy of inventory quantities against the ordered amount;
 - Confirmed proper documentation and monitoring of expiration dates for stocked inventory;
 - Verified the FIFO method for inventory storage, with newer items at the back and older ones at the front of the refrigerator unit;
 - Confirmed adherence to established protocols for documenting damaged goods, short shipments, and discrepancies;
 - Verified timely temperature readings and documentation (within Redbook) for frozen and refrigerated inventory upon receipt;
 - Assessed equipment conditions and prompt reporting of inoperable equipment to the relevant department for maintenance;
 - Inspected cash boxes and safes to confirm adherence to proper handling procedures for cash safeguarding.
- Assessed inventory procurement processes, including examining requisition procedures, delivery protocols, and compliance measures.
- Reviewed the organization's policies and procedures, including distribution and frequency of Board/Local Nutrition Services updates.
- Reviewed the FY2022 fixed asset verification procedures for NSD for completeness and accuracy. Verified the documentation and disposition of assets and validated the proper recording of proceeds from asset sales in the financial system.
- Evaluated the accuracy and completeness of three-way match processing (invoice, goods receipt, and order) to confirm validated invoices were processed for payment.
- Reviewed the due diligence efforts completed before outsourcing NSD functions.

Reporting

At the conclusion of this internal audit, we summarized our findings into this report. We have reviewed the results with the appropriate Management personnel and have incorporated Management's responses into this report.



OBSERVATIONS MATRIX

Observation	1. Inventory Management: Hazardous Cleaning Supplies															
<p style="text-align: center;">High</p>	<p>Per the 2023-2024 Hazardous Analysis Critical Control Point (“HACCP”) Plan and Standard Operating Procedures—300 Cleaning and Sanitizing, all hazardous cleaning supplies should be stored in a clear, designated area physically separated from areas where food is stored, prepared, or served.</p> <p>RSM conducted site visits at eight (8) locations to observe current inventory management procedures and compliance with procedural requirements. During our site visits, the following was identified:</p> <ul style="list-style-type: none"> One (1) of the eight (8) sites visited did not properly store hazardous cleaning supplies in a clear, designated area physically separated from areas where food is stored, prepared, or served. We observed several bottles of bleach were stored on a shelf adjacent to packaged foods and produce in the pantry. <p>Inadequate storage of hazardous cleaning supplies may lead to unintended contamination or chemical reactions with food items and ingredients.</p>															
<p>Recommendation</p>	<p>HISD NSD should consider the following recommendation:</p> <ol style="list-style-type: none"> The NSD should consider enhancing current required employee training on handling, storage, and use of hazardous cleaning supplies. This training should also be part of new employee onboarding orientation. 															
<p>Management Action Plan</p>	<p>Response: Cleaning supplies were present on the bottom shelf in the storage area. Action was taken immediately when HISD was alerted to this situation at the school.</p> <table border="1" data-bbox="403 881 940 1047"> <thead> <tr> <th colspan="2">Shelving Layout at time of Observation</th> </tr> </thead> <tbody> <tr> <td>Paper Goods</td> <td>Food</td> </tr> <tr> <td>Cleaning Supplies</td> <td>Food</td> </tr> </tbody> </table> <table border="1" data-bbox="1010 881 1482 1047"> <thead> <tr> <th colspan="2">NEW Shelving Layout</th> </tr> </thead> <tbody> <tr> <td>Paper Goods</td> <td>Food</td> </tr> <tr> <td>Paper Goods</td> <td>Food</td> </tr> </tbody> </table> <table border="1" data-bbox="1547 881 1887 1047"> <thead> <tr> <th>New Rack</th> </tr> </thead> <tbody> <tr> <td>Cleaning Supplies</td> </tr> <tr> <td>Cleaning Supplies</td> </tr> </tbody> </table> <p>Completed:</p> <ol style="list-style-type: none"> QC inspection at this school conducted (part of the routine schedule) on January 25, 2024 - issue was still resolved. City of Houston Health Department Inspection on February 22, 2024 - this issue was still resolved. <p>Ongoing:</p> <ol style="list-style-type: none"> Training for all Team Leads at L.E.A.D training. Monitored for compliance routinely with internal inspection , conducted by the HISD NS Quality Control Specialists. Monitored for compliance routinely with bi-annual City of Houston Health Inspections. <p>Additional Training: Scheduled to be conducted to all Team Leads April 16-18, 2024 during the monthly Team Lead meeting.</p> <p>Responsible Party: Nutrition Services Operations.</p> <p>Estimated Completion Date: Initial correction and follow up audits have been completed. This is an ongoing training topic for the department and Team Leads.</p>	Shelving Layout at time of Observation		Paper Goods	Food	Cleaning Supplies	Food	NEW Shelving Layout		Paper Goods	Food	Paper Goods	Food	New Rack	Cleaning Supplies	Cleaning Supplies
Shelving Layout at time of Observation																
Paper Goods	Food															
Cleaning Supplies	Food															
NEW Shelving Layout																
Paper Goods	Food															
Paper Goods	Food															
New Rack																
Cleaning Supplies																
Cleaning Supplies																



OBSERVATIONS MATRIX (CONTINUED)

Observation	2. Inadequate Fixed Asset Verification
<p style="text-align: center;">High</p>	<p>Asset verification is a process designed to confirm an organization's assets' existence, location, and condition. HISD standard procedures include the proper creation of the Fixed Asset Listing, physical inspection of the asset's existence onsite, documentation via photograph, tie-out to asset tag, identification of any discrepancies or missing assets, and communicating all findings to the Fixed Asset Department ("FAD") to update the status of the assets accurately. In cases where discrepancies are identified, ongoing communication with FAD should persist until the asset status is resolved.</p> <p>RSM inquired and identified that a Fixed Asset Verification was not conducted for FY 2023. According to Food Services Attendant Team Lead ("Team Lead"), staff limitations prevented the verification from being completed.</p> <p>The most recent fixed asset verification was performed in FY 2022. RSM acquired the documentation to substantiate that the fixed asset verification conducted complied with District policy and noted the following:</p> <ul style="list-style-type: none"> • The NSD department did not designate an employee to manage the fixed asset verification process to validate its overall completeness and accuracy. Additionally, the NSD did not provide the results of the fixed asset verification to the FAD. • 54 out of 131 fixed assets did not have sufficient supporting documentation to confirm the existence or identify the condition of the fixed asset: The total book value of the associated 54 assets amounted to \$32,299, compared to the overall book value of all 131 assets, which amounted to 40,358. <ul style="list-style-type: none"> ○ 41 fixed assets lacked adequate photos to confirm their existence. ○ 13 fixed assets did not include or had inconsistent serial or tag numbers. <p>The prompt submission of fixed asset verification results to the Fixed Asset Accounting Department facilitates timely and efficient asset management, including the sale, scrapping, or disposal of accurately identified assets. This practice promotes the integrity of asset records, supports compliance with financial and audit standards, and enhances the organization's decision-making and operational efficiency through accurate financial reporting.</p>
<p style="text-align: center;">Recommendation</p>	<p>HISD NSD should consider the following recommendation:</p> <ol style="list-style-type: none"> 1. NSD should designate a dedicated employee within the department to manage the fixed asset verification process proactively. This selected individual should be responsible for ensuring the overall completeness and accuracy of the assessment. Upon validation, results should be communicated to the Fixed Asset Department, enabling action on assets to be sold, scrapped, or removed, thus streamlining asset management and reinforcing financial record integrity. 2. The Fixed Assets Manager should conduct training sessions with NSD Leadership to establish explicit guidelines, procedures, and resource provisions for the effective execution of fixed asset verification procedures.
<p style="text-align: center;">Management Action Plan</p>	<p>Response: NS Department will take on this responsibility and partner with Fixed Asset Management.</p> <p>Responsible Party: Fixed Asset Management and NSD.</p> <p>Estimated Completion Date: NS Department will conduct the Fixed Asset Verification, schedule to be completed by end of FY 2024 and then annually moving forward</p>



OBSERVATIONS MATRIX (CONTINUED)

Observation	3. Insufficient Cash Safeguarding
Moderate	<p>Cash used during serving hours is limited to petty cash and is stored within safe boxes within Team Lead offices at each location. Access to the safe boxes is granted through codes issued to Team Leads, School Principals, and Operations Coordinators. At times, custodians and school principals have access to the keys to the kitchen area, where Team Lead offices are located, but they do not have access to the safe codes themselves. It is important to note that the amount of petty cash differs among schools based on the consumption volume at each location.</p> <p>RSM conducted site visits at eight (8) locations to observe current cash safeguarding procedures and validate compliance with HISD's requirements. During our site visits, the following was identified:</p> <ul style="list-style-type: none"> Two (2) of the eight (8) sites had unlocked safe boxes within the Team Lead's office that housed petty cash. <p>Ineffective safeguarding of safe boxes increases the risk of unauthorized access, potential theft, and misappropriation of funds.</p>
Recommendation	<p>HISD NSD should consider the following recommendations:</p> <ol style="list-style-type: none"> Reinforce the importance of secure cash storage by updating and distributing specific guidelines on safe box access and locking procedures. Initiate training for Team Leads and staff to promote strict compliance with cash handling protocols.
Management Action Plan	<p>Response: Safes are required to be locked when not in use.</p> <p>NS SOP and Training:</p> <ol style="list-style-type: none"> This is currently part of the NS Cash Handling Agreement. However, to improve compliance, the NS Cash Handling Agreement will be updated to provide more clarity on this standard. Training and reinforcing this SOP will occur April 16-18 during the Team Lead training. <p>Responsible Party: Nutrition Services Operations</p> <p>Estimated Completion Date: April 19, 2024</p>



OBSERVATIONS MATRIX (CONTINUED)

Observation	4. Inventory Management: Inconsistent Order Discrepancy Process
<p>Low</p>	<p>When receiving goods from outside vendors, the designated Team Lead verifies all received goods match the corresponding invoice and reconciles them with the total order amount. If a discrepancy arises between the invoice and the order, the Team Lead records the discrepancy using the Discrepancy Form. Subsequently, the form is archived, and an email containing the form is sent to the Operations Coordinators.</p> <p>RSM conducted site visits at eight (8) locations to observe current inventory receipting procedures and validate compliance with HISD's procedural requirements. During our site visits, the following was identified:</p> <ul style="list-style-type: none"> • Five (5) of the eight (8) sites failed to accurately document identified order discrepancies on the Outside Vendor Discrepancy & Credit/Return form and provide these forms to the Operations Coordinators. At all sites visited, the Team Lead communicated the discrepancy through text, phone calls, or emails, but the required forms were neither completed nor forwarded to the Operations Coordinators. It is important to note that all discrepancies identified in this process were considered insignificant and would not cumulatively constitute a material difference, such as the absence of just one unit of a particular product. <p>Team Leads District-wide should have a standard and consistent process for inventory receipt and discrepancy procedures. The issues noted above indicate a need for enhanced training on correctly using documentation forms. When an order discrepancy is identified, the Team Lead should document all differences within PrimeroEdge (Primero), the District's cloud-based nutrition system, complete the Outside Vendor Discrepancy & Credit/Return Spreadsheet, and notify the Operation Coordinator via email.</p> <p>Inadequate documentation and communication of discrepancies highlight operational inefficiencies, which could lead to unrecouped funds due to overpayments or incorrect shipments, strained vendor relations, and inventory inaccuracies.</p>
<p>Recommendation</p>	<p>HISD NSD should consider the following recommendations:</p> <ol style="list-style-type: none"> 1. Conduct training sessions with Team Leads to establish clear guidelines, procedures, and resources to accurately reconcile invoice amounts, total order amounts, and receipt amounts within Primero. 2. Establish a consistent process for documenting the "Outside Vendor Discrepancy & Credit/Return Spreadsheet." A clear documentation protocol should be established for instances where items received do not align with the invoice.
<p>Management Action Plan</p>	<p>Response: The process for completing the Outside Vendor and Discrepancy & Credit/Return Form will have an established process.</p> <p>NS SOP and Training:</p> <ol style="list-style-type: none"> 1. The process for completing the Outside Vendor and Discrepancy & Credit/Return Form will be using the online version. Operations Coordinators will assist the Team Leads if there are questions with the form. Training for all Team leads will also be provided. 2. Training and reinforcing this SOP will occur April 16-18 during the Team Lead training. <p>Responsible Party: Nutrition Services Operations</p> <p>Estimated Completion Date: April 19, 2024</p>



OBSERVATIONS MATRIX (CONTINUED)

Observation	5. Inventory Management: Deviation from First-In-First-Out (FIFO) Procedures
Low	<p>Team Leads are tasked with verifying that incoming goods from external vendors match the corresponding invoice and order totals. Post-verification, kitchen staff must document critical information, such as SAP numbers, expiration dates, and delivery dates, on a copy of the signed invoice before employing the FIFO (First In, First Out) method for storage.</p> <p>RSM conducted site visits at eight (8) locations to observe current inventory management procedures and validate compliance with HISD's procedural requirements. During our site visits, the following was identified:</p> <ul style="list-style-type: none"> One (1) of the eight (8) sites had freezer space constraints, necessitating inventory reorganization. Instead of adhering to the FIFO methodology, items were arranged based on size or capacity. <p>Failure to follow FIFO inventory methods may increase the risk of inventory mismanagement, including inaccuracies and spoilage.</p>
Recommendation	<p>HISD NSD should consider the following recommendations:</p> <ol style="list-style-type: none"> Provide targeted training for Team Leads and kitchen staff on the importance of adhering to the FIFO method to validate inventory integrity and minimize waste. Procedures should also be designed for handling inventory management when non-routine matters occur, such as the event noted above. Enhance monitoring of inventory levels to minimize duplications and efficiently manage freezer space. If necessary, consider evaluating the need for additional deliveries for specific locations based on storage capacities and business needs.
Management Action Plan	<p>Response: The kitchen has been supported with reorganizing and sorting of the frozen items. An analysis has also been completed regarding frequency of deliveries.</p> <p>Ongoing Maintenance: Monitored for compliance routinely with internal inspections, conducted by the HISD NS Quality Control Specialists.</p> <p>Additional Training: FIFO training is scheduled to be conducted to all Team Leads during the one of monthly Team Lead meetings held throughout the year.</p> <p>Responsible Party: Nutrition Services Operations</p> <p>Estimated Completion Date: Initial correction and follow up inspections have been completed. This is an ongoing training topic for the department and Team Leads.</p>



OBSERVATIONS MATRIX (CONTINUED)

Observation	6. Inventory Management: Inconsistent Food Temperature Practices
<p>Low</p>	<p>Per the 2023-2024 HACCP Plan and Standard Operating Procedures, the Team Lead within each school is required to confirm the temperature of frozen or refrigerated food within the “Redbook.” Redbook is a food safety training program that covers critical topics such as hazard analysis, allergens, sanitation, and food handling practices and is a primary tool for complying with regulatory requirements. Redbook receiving requirements state frozen products should be at 32 degrees Fahrenheit or below, and refrigerated products should be at 41 degrees Fahrenheit or below.</p> <p>RSM conducted site visits at eight (8) locations to observe current inventory receipting procedures and to validate accordance with HISD’s procedural requirements. During our site visits, the following was identified:</p> <ul style="list-style-type: none"> • One (1) of the eight (8) sites visited measured the temperature of the inventory after the items were stored in the freezer for approximately ten minutes instead of obtaining the temperature of the goods upon delivery from the vendor, which raises the likelihood of the temperature check proving ineffective, as the product may undergo temperature fluctuations between the time of delivery and the actual probing of the item. <p>Timely receipt and accurate temperature monitoring of frozen goods are crucial for food safety. They prevent the growth of microorganisms and reduce the risk of foodborne illnesses. By maintaining these practices, the organization actively supports regulatory compliance, preserves food quality, and safeguards consumer health and satisfaction, minimizing legal and financial risks.</p>
<p>Recommendation</p>	<p>HISD NSD should consider the following recommendations:</p> <ol style="list-style-type: none"> 1. Provide training to kitchen staff to reinforce the importance of adhering to proper storage practices and preventing the use of spoiled inventory. 2. The Operations Coordinator responsible for specific zones within the District should enforce and oversee adherence to food safety standards, including immediately measuring temperatures for frozen and refrigerated products before storage. This will not only improve food safety but also optimize the storage conditions of perishable items.
<p>Management Action Plan</p>	<p>Response: Receiving the deliveries and putting cold food away quickly is critical for food safety. Taking the temperatures at the time of delivery will be reinforced to the kitchen staff.</p> <p>Ongoing Maintenance: Monitored for compliance routinely with internal inspections, conducted by the HISD NS Quality Control Specialists.</p> <p>Additional Training: Training and reinforcing this SOP occurred March 19-21 during the Team Lead training.</p> <p>Responsible Party: Nutrition Services Operations</p> <p>Estimated Completion Date: Initial correction and follow up audits have been completed. This is an ongoing training topic for the department and Team Leads.</p>

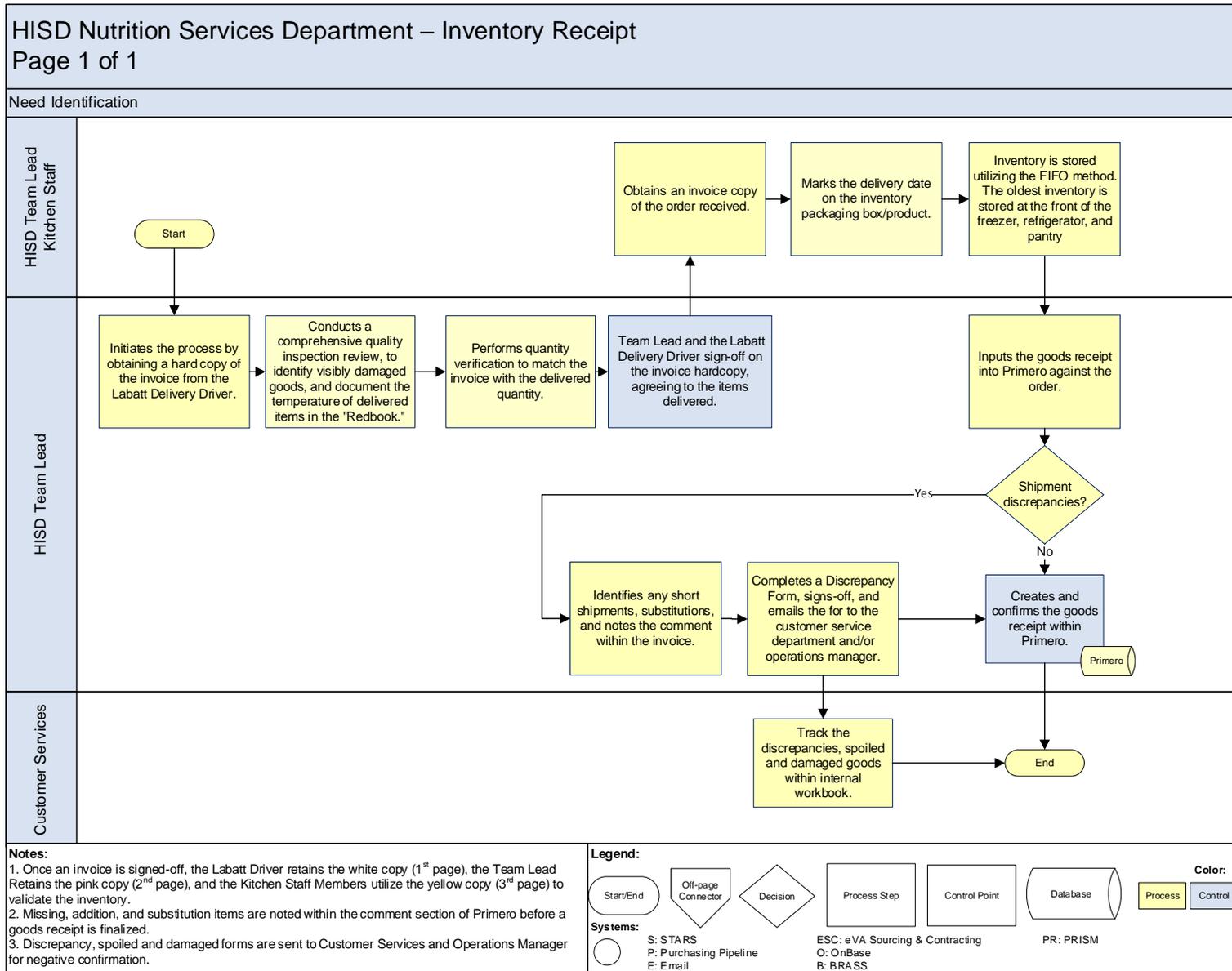


OBSERVATIONS MATRIX (CONTINUED)

Observation	7. Utilization of Bennington Warehouse Facilities
Low	<p>Based on an RSM site visit and management inquiry, the Hexser T. Holliday Food Services Support Facility (“Bennington Warehouse”), located at 6801 Bennington St, Houston, TX 77028, is underutilized with significant annual costs. Therefore, opportunities to better utilize the space (i.e., reconfigure, transform, sell, etc.) may exist and should be considered against current expenses and utilization.</p> <p>The Bennington Warehouse, previously central to the NSD in-house food production, food/supply warehousing and operations, has been decentralized to school kitchens, where the Broadline Distributor delivers food and goods to each kitchen and the NSD personnel prepare, cook, and serve the meals to the students. Based on inquiry and an on-site visit, 158,400 square feet (80%) of the first floor of the building is underutilized or unnecessary based on current operations. FY 2023, expenditures for the Bennington Warehouse amounted to \$4,348,980. The underutilization of the 219,000-square-foot Bennington Warehouse and its maintenance costs presents HISD with financial and operational challenges and underscores several opportunity costs.</p>
Recommendation	<p>HISD NSD should consider the following recommendation:</p> <ol style="list-style-type: none"> 1. Perform a cost-benefit analysis of the Bennington Warehouse. This analysis should evaluate current and potential uses' economic impact, including repurposing the real property or equipment for District needs or sale. The findings should guide strategic decisions to enhance resource allocation towards the primary objectives of the NSD and improve overall District efficiency.
Management Action Plan	<p>Response: The Office of the Chief Financial and Operations Officer, in collaboration with NSD, acknowledges the findings from the internal audit regarding the underutilization of the Bennington Warehouse. We understand the purpose for which the building was originally built has changed. The change in the purpose of the building has caused this building to be underutilized and thus become surplus. We realize the financial impact to the general operating budget. We are in the process of moving NSD to a more suitable site. This process for NSD has begun. In the future, we will take to the Board of Managers a listing of this building as surplus property to approve for auction and sale.</p> <p>Responsible Party: Chief Financial and Operations Officer</p> <p>Estimated Completion Date: June 30th 2025</p>

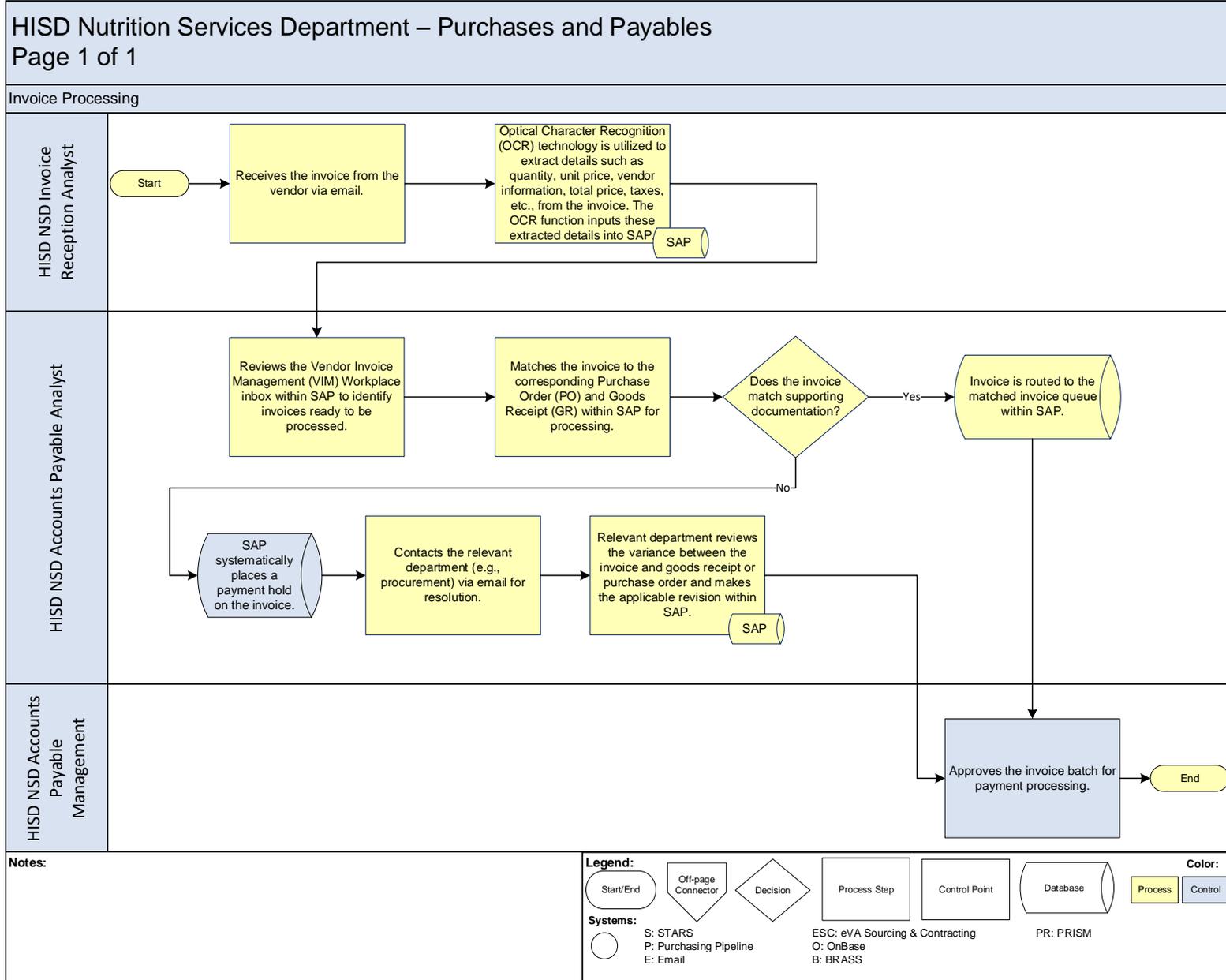


APPENDIX A – INVENTORY RECEIPT





APPENDIX A – INVOICE PROCESSING





RSM US LLP
1330 Post Oak Blvd
Suite 2400
Houston, TX 77056
713.625.3500

www.rsmus.com

RSM US LLP is a limited liability partnership and the U.S. member firm of RSM International, a global network of independent audit, tax and consulting firms. The member firms of RSM International collaborate to provide services to global clients, but are separate and distinct legal entities that cannot obligate each other. Each member firm is responsible only for its own acts and omissions, and not those of any other party.

For more information, visit rsmus.com/aboutus for more information regarding RSM US LLP and RSM International.

© 2024 RSM US LLP. All Rights Reserved.