

8/22/05 Copy to Michele, Kadie, Phil, Rick, Pam, Robin, Celestina, Lisa, File

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United States Department of Agriculture
Food and Nutrition Service

Midwest Region

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Reply to
attn of: MWSSNP 2-3; WC 7-1; WC 5-1 August 8, 2005

Subject: Guidance for WIC Policy Memorandum #2004-4
Implementation of the Infant Formula Cost Containment
Provisions of P.L. 108-265 – Rebate Invoices

To: State WIC Directors
Midwest Region

This memorandum serves as guidance for State agencies to develop procedures that ensure infant formula rebate invoices provide a reasonable estimate (or actual count) of the number of units of contract brand infant formula sold to participants, as required by the Child Nutrition and WIC Reauthorization Act of 2004 (Reauthorization Act). While we understand State agencies have already implemented this provision, the information provided in this guidance may further assist State agencies in providing accurate data to infant formula manufacturers in their rebate invoices.

Background

The Reauthorization Act (Public Law 108-265), enacted June 30, 2004, contains provisions related to infant formula cost containment practices. One of the provisions pertains to infant formula rebate invoices. It reads as follows:

Section 203(e)(5) of the Reauthorization Act amends Section 17(h)(8)(A) by adding the following:

“(vi) REBATE INVOICES.—Each State agency shall have a system to ensure that infant formula rebate invoices, under competitive bidding, provide a reasonable estimate or an actual count of the number of units sold to participants in the program under this section.”

This provision was effective October 1, 2004. A policy memorandum (2004-4) was issued August 9, 2004, relaying the provision. In addition, a final regulation is scheduled to be published this year codifying this provision.

Nationally, over the past several years FNS has worked with a number of State agencies that have developed procedures to more accurately estimate the number of units of contract infant formula being purchased. In preparation for providing this guidance, FNS also sought input from the National WIC Association (NWA) and infant formula manufacturers. Specifically, FNS requested information on procedures and/or best practices in State agencies that provide a reasonable estimate of contract brand infant formula purchases.

We acknowledge that it is not realistic to assume that only one methodology exists and/or is appropriate for all State agencies to use when determining a reasonable estimate of the number of units of contract brand infant formula sold to WIC participants. Nevertheless, State agencies should develop a methodology based on their own capabilities and mutually agreed upon by all parties. Implementing new procedures may

require State agencies to spend nutrition services and administration funds, especially for start up costs. State agencies should be encouraged to apply for operational adjustment funds and/or general infrastructure grants to offset some of these costs.

Methodologies

The National WIC Association and all three manufacturers responded to our request for best practices currently used by State agencies to estimate the number of units of contract brand infant formula sold to participants. One manufacturer sent a listing of methodologies they believe are acceptable practices to meet this requirement. The attached chart was developed based on that list. Two manufacturers suggested methods requiring the State agency to determine the average retail price of a unit of infant formula under contract. The basis of analysis for the retail price information can be the vendor, vendor peer group, or a State-wide average price. Under this approach, the total redeemed dollar amount of the food instrument is divided by the calculated average retail price to obtain an estimate of units of contract brand infant formula sold. This estimate of units sold would be used as the basis for the monthly rebate invoice. Regardless of the specific method used, State agencies should isolate infant formula purchases by issuing separate food instruments for infant formula; other additions to the food instrument, such as infant cereal or juice, distort the calculation.

Other methodologies can be used to obtain an actual count of units of contract brand infant formula sold. These include: 1) electronic benefits transfer systems which allow the State agency to know exactly how many units of infant formula are purchased; and (2) requirements for the vendor to write the number of units purchased directly on the food instrument during the transaction. The rebate invoice would be based on the number of units written on the food instruments.

Supporting Data

In addition to developing a methodology as discussed above, it is important that State agencies provide as much information as necessary to support monthly rebate invoices without violating vendor or participant confidentiality. FNS has always supported State agencies providing data on a monthly basis that supports the rebate invoice. Providing such information allows the manufacturer to verify the monthly rebates in a timely manner. It also reduces the need for an audit by the manufacturer and, as such, should allow State agencies ample time to closeout in a timely fashion. FNS encourages State agencies to provide, on a monthly basis, the following:

- Food instrument number
- Pseudo vendor identification number
- Food package identification number or code
- Product name (including physical form)
- Number of units authorized to purchase
- Effective date of food instrument
- Redemption date of food instrument
- Redeemed amount

In closing, we hope this information is helpful when developing procedures to ensure infant formula rebate invoices provide a reasonable estimate of the number of units purchased. However, we do not believe this information is exclusive. We encourage State agencies to continue working with the regional office and infant formula manufacturers to develop systems that are mutually satisfactory.

If you have any questions, please contact Rochelle Sheets of my staff at (312) 353-3848.

A handwritten signature in cursive script that reads "Julie Mikkelson". The signature is written in black ink and is positioned above the printed name.

JULIE MIKKELSON
Regional Director
Special Supplemental Nutrition Programs

Attachment

Infant Formula Rebate Invoice Systems: Potential Methods to Provide an Actual Count or Reasonable Estimate of the Number of Units Sold

The systems below describe methods to obtain a reasonable estimate or an actual count of the number of contract brand infant formula units sold to participants in the program, as required by the Child Nutrition and WIC Reauthorization Act of 2004 (Section 17(h)(8)(A)).

Methods to Obtain an Actual Count:

Electronic Benefits Transfer (EBT)

The quantity of units purchased is automatically captured at the point of sale as part of the WIC transaction. Redemption data are compared to issued data and subsequently billed to the contractor on a monthly basis.

Retail Quantity Capture

The purchased quantity of units is recorded by the retailer on the food instrument. This quantity is then entered into the billing database during the banking process and captured by the data processor. The manufacturer is then billed monthly for the actual units purchased.

Data Required	Data Source
Quantity purchased	Recorded by retail clerk
Quantity purchased	Captured by check processor
Quantity purchased	Billing module

Methods to Obtain a Reasonable Estimate

Outlier Analysis

The State agency performs a statistical analysis of the redeemed amount for each food instrument type for each vendor to identify redeemed amounts that are outliers. If the result is lower than the expected redeemed amount, the instrument is likely to have been redeemed for fewer units than the authorized quantity. An analysis is then done to determine the likely quantity purchased using the expected price per unit. State agencies should isolate infant formula purchases by issuing separate food instruments for infant formula.

Data Required	Data Source
Redeemed dollar amount	Each food instrument, each vendor
Normal redeemed amount	Calculated by billing module
Redeemed quantity	Calculated by billing module

Vendor Price Table

The State agency develops a database containing each vendor's actual reported prices for each rebated contract infant formula item. Such data should be collected on an annual or more frequent basis. These prices are then used to calculate the purchased quantity for each food instrument by dividing the redeemed amount by the vendor's price for that item. These quantities are then used to generate the monthly rebate invoice. State agencies should isolate infant formula purchases by issuing separate food instruments for infant formula.

Data Required	Data Source
Vendor's price for item	Each retail vendor
Redeemed dollar amount	Each food instrument
Redeemed quantity	Calculated by billing module

Vendor Most Probable Price

For each month, each vendor's most likely price per unit of infant formula is determined by dividing the total redeemed amount by the issued quantity of contract infant formula for each food instrument. The resulting calculated prices are analyzed to determine the mode (the most frequently occurring price) of each vendor for each contract formula product. That most likely price is used to determine the purchased unit quantity for each redeemed food instrument by dividing the total value of the food instrument redeemed by the most likely price. Any fraction is dropped. This quantity, not to exceed the quantity authorized for issuance on the food instrument, is then used to generate a monthly rebate invoice. State agencies should isolate infant formula purchases by issuing separate food instruments for infant formula.

Data Required	Data Source
Redeemed amount	Each food instrument
Issued quantity	Data base
Most likely vendor item price	Calculated by probability table
Redeemed quantity	Calculated by billing module

Vendor Peer Group Price

Establish peer groups based on some criteria related to pricing, such as size of the establishment or number of cash registers. On an annual or more frequent basis, determine an average retail price for each rebated item in each peer group. Use that price to determine the purchased quantity by dividing the redeemed amount of each food instrument by the vendor peer group price. Any fraction is dropped. This quantity, not to exceed the quantity authorized for issuance on the food instrument, is then used to generate the monthly rebate invoice. State agencies should isolate infant formula purchases by issuing separate food instruments for infant formula.

Data Required	Data Source
Vendor Peer Group	State WIC files
Store prices	State WIC files
Vendor peer group item average price	State WIC files – calculated from store data
Redeemed dollar amount	Each food instrument
Redeemed quantity	Calculated by billing module

Average Price

Determine an average retail price per unit for each rebated item. This could be determined by the State agency based on reliable information or purchased from a third party like A.C. Nielsen. The redeemed amount on each food instrument is divided by that average retail price to determine the quantity of units purchased. Any fraction is dropped. This quantity, not to exceed the quantity authorized for issuance on the food instrument, is then used to generate the monthly rebate invoice. State agencies should isolate infant formula purchases by issuing separate food instruments for infant formula.

Data Required	Data Source
Average price	Purchased or calculated by State agency
Redeemed dollar amount	Each food instrument
Redeemed quantity	Calculated by billing module

Calculated Discount With Periodic Adjustment

Use a percentage discount rate derived from an annual or more frequent audit and agreed to by the manufacturer and the State agency. That rate would be applied to each monthly invoice. This audit could apply any of the preceding methods, but would only calculate and adjust the rate periodically instead of continually. The percentage could be calculated either prospectively or retrospectively.