DECISION

THE COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

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FILE: B-178564 DATE: JAN 21 1976

MATTER OF: Project E.A.T.

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DIGEST: Ordinarily, expenditures of service institution in providing free meals to needy children under National School Lunch Act may not be reimbursed where regulatory requirement of obtaining tax exempt certification from Internal Revenue Service was not met. However, GAO will not object to payment under particular facts of this case since needy children were actually fed if Secretary of Agriculture determines that service institution was nonprofit as required by statute and that failure to obtain certification was result of good faith misunderstanding.

The Department of Agriculture (USDA) has requested a decision from this Office concerning the propriety of reimbursing a Summer Special Food Service Program sponsor, Project E.A.T. of San Diego, California for expenses incurred in feeding needy children from June 16 to July 31, 1975.

The program is authorized by section 13 of the National School Lunch Act, as amended, 42 U.S.C. § 1761, which provides Federal assistance to approved public or private non-profit service institutions (sponsors) who furnish specified food services to needy children at approved lunch sites. The program is administered at the Federal level by the Food and Nutrition Service (FNS) of the Department of Agriculture which in turn operates through designated State agencies (with certain exceptions not here relevant).

Project E.A.T. (Environmental Advocates Together), a service organization, applied to the State of California Department of Education Office of Food Nutrition Services (OFNS), (which is the designated State agency to administer the program in the State of California) for participation as a sponsor in the Summer Special Food Service Program. On June 12, 1975, Daniel A. Tanner, the Executive Director of Project E.A.T. signed a sponsor's agreement with OFNS to conduct the program and was provided an initial advance authorization of $350,000 later increased to $700,000.

Project E.A.T. provided food services at fifty-four approved sites from June 16 until July 31, 1975, at which time the program was terminated by the OFNS. The termination was based on the results of a USDA preliminary review of program operations that uncovered possible mismanagement problems and also because of new information which indicated that Project E.A.T. lacked tax exempt status, as required by law and regulation. The USDA had not issued a final report of its findings as of this date.

Project E.A.T.'s claims for reimbursement during the period of operation totals $310,445.49 on the basis of units served plus an administration charge, and $323,802.88 on the basis of 80 percent of reported cash and in-kind expenditures. Because of the termination, however, none of Project E.A.T.'s claims have been paid up to this date. Since Project E.A.T. is currently unable to meet its financial obligations to food suppliers and other program creditors, the USDA has requested that the California Department of Education be permitted to pay the claims of Project E.A.T. for June, 1975, so that it may satisfy some of the obligations it incurred in carrying out the Summer Special Food Service Program. The USDA submits that any overclaim based on program mismanagement that may be developed against Project E.A.T. could be covered by withholding payment of the July claim.

In order to pay even the June portion of the program expenses, it is necessary to find that the statutory and regulatory prerequisites have been met. Section 1761(a)(2) of title 42, United States Code, requires that eligible sponsors be service institutions which are public or private non-profit institutions. The USDA regulations, 7 C.F.R. § 225.2(M) provide as follows:

> "Private nonprofit service institution means a nonpublic service institution that is exempt from income tax under the Internal Revenue Code, as amended.

Section 225.76 of the regulations requires each private service institution to attach to its application for program sponsorship an Internal Revenue Service (IRS) certification of its non-profit status.

The problem is that it does not appear that Project E.A.T. has obtained an IRS tax-exempt status ruling. Project E.A.T. felt that it had obtained tax exempt status under the "corporate cover" of the San Diego Jobs for Progress, Inc. (known as Operation Ser). Operation Ser has a "group ruling" under which it, as a parent organization, can

sponsor subordinate units and cover them under its tax exempt ruling. This group ruling for Operation Ser was submitted with Project E.A.T.'s application to support its assertion of tax exempt status. Auditors from the Department of Agriculture found that at least as of July 8, 1975, some type of an agreement, formal or informal, did exist between Operation Ser and Project E.A.T. for the use of the IRS tax exemption number assigned to Operation Ser. However, it also appears that Operation Ser did not officially extend its certificate to cover Project E.A.T. and is not now willing to do so. It was on the basis of this evidence that the California Department of Education concluded that Project E.A.T. did not have tax exempt status and so terminated the project on July 31, 1975. In his submission to us, the Assistant Secretary of Agriculture states:

> "* * * it is apparent from information developed by the auditors that the failure to obtain IRS tax exempt certification was the result of a misunderstanding on the part of Project E.A.T. and not an attempt to defraud the government* * *."

Ordinarily, the expenditures of a service institution such as Project E.A.T. in providing free meals to needy children under section 13 of the National School Lunch Act, as amended, may not be reimbursed when regulatory requirements were not met. However, it is clear that a substantial number of meals were actually provided to needy children. Also, any payments made would go to the liquidation of financial obligations incurred by Project E.A.T. in the operation of the Summer Special Food Service Program. Therefore, if the Secretary of Agriculture determines that the statutory requirement that the service institution be nonprofit has been met; that the regulatory requirement that the service institution be tax exempt has been substantially complied with; and that Project E.A.T.'s failure to obtain a tax exemption certification was the result of a good faith misunderstanding, we would not object to some payment to Project E.A.T. based on the special facts of this situation. A finding that it had substantially complied with the tax-exempt status requirement should involve a determination that Project E.A.T. is an organization of the type described in 26 U.S.C. § 501 (1970) as being tax exempt and that it would have been eligible for tax-exempt certification if it had either applied for one from the Internal Revenue Service or been extended coverage under Operation Ser's "group ruling."

In his submission the Assistant Secretary advises that termination of the program was also based on possible mismanagement on the part of Project E.A.T. and that the Office of Audit of the Department

of Agriculture is auditing the program's records to determine compliance with program regulations and the amount of reimbursement that could properly be paid had Project E.A.T. had a tax-exempt certification.

The Assistant Secretary further states that claims have been submitted for June and July and that it appears that any overclaim based on program mismanagement could be adequately covered by withholding payment of the July claim. On this basis it is suggested that paying the June claim would allow Project E.A.T. to make some payment to its creditors for costs incurred in the operation of the program.

Based on the Assistant Secretary's assurances that the Government's interests would be protected and that Project E.A.T. has earned reimbursement of at least that amount through providing qualified meals and since the payment will essentially be for the purpose of making some payment to its creditors, we would not object to payment as proposed. However, in view of the possible mismanagement of this program, we believe the Department of Agriculture should carefully analyze available evidence as to the amount of meals actually provided by Project E.A.T. See, for example, our decisions of December 5, 1972, and August 14, 1974, to the Secretary of Agriculture in the Matter of the Claim of United Bronx Parents Association, B-176994.

R.F. KELLER

Deputy Comptroller General
of the United States