

# Proposed Rules

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This section of the FEDERAL REGISTER contains notices to the public of the proposed issuance of rules and regulations. The purpose of these notices is to give interested persons an opportunity to participate in the rule making prior to the adoption of the final rules.

## DEPARTMENT OF AGRICULTURE

### Food and Nutrition Service

#### 7 CFR Part 250

RIN 0584-AD08

#### Codification of Poultry Substitution and Modification of Commodity Inventory Controls for Recipient Agencies

**AGENCY:** Food and Nutrition Service, USDA.

**ACTION:** Proposed rule.

**SUMMARY:** This rule concerns the types of foods that may be available from the Department of Agriculture for any of the uses authorized under the Food and Nutrition Service's Food Distribution Programs and the manner in which those foods must be labeled. The first part of the rule will allow limited poultry substitution and full fruit, vegetable, and egg substitution in the processing program. The second part of the rule deals with the reduction of commodity inventory controls for schools to allow use of commercial labels.

The Department has operated a demonstration project program since Feb. 1, 1996, which allows commercial poultry to be substituted for commodity poultry in processing, in order to expedite and improve that program. The data gathered from recipient agencies, Agriculture Marketing Service (AMS) graders, and the AMS procurement division has been positive. Substitution of commercial fruits, vegetables, and eggs for commodity fruits, vegetables, and eggs has been allowed under 7 CFR 250.30(f)(4) for over ten years.

During that time, required Certified Public Accountant (CPA) audits have not shown any significant problems with fruit, vegetables, or egg substitution. There has been no substitution of inferior product identified. Therefore, this proposed rule seeks to change the regulations to allow limited poultry substitution and full fruit substitution, vegetable substitution,

and egg substitution on a permanent basis.

Secondly, because of changes in the commercial market and the food donation programs, the Department will allow vendors to use their own labels in place of USDA donated food labels for school programs. Commercial labels have already been introduced in other USDA food donation programs with good results, and commercial labels for school commodities have been permitted on select commodities going into schools. However, commercial labels complicate the inventory procedures currently utilized in schools. Therefore, FNS is proposing to modify the current inventory requirements for schools in order to accommodate the use of commercial labels.

**DATES:** Comments regarding this proposed rule should be submitted by April 22, 2002.

**ADDRESSES:** Comments should be sent to Suzanne Rigby, Chief, Schools and Institutions Branch, Food Distribution Division, Food and Nutrition Service, U.S. Department of Agriculture, 3101 Park Center Drive, Alexandria, Virginia 22302-1594. Comments in response to this request may be inspected at 3101 Park Center Drive, Alexandria, Virginia, during normal business hours (8:30 a.m. to 5 p.m., Mondays through Fridays).

**FOR FURTHER INFORMATION CONTACT:** Suzanne Rigby at the above address or telephone (703) 305-2644.

#### SUPPLEMENTARY INFORMATION:

##### Executive Order 12866

This proposed rule has been determined to be not significant for purposes of Executive Order 12866 and, therefore, has not been reviewed by the Office of Management and Budget.

##### Public Law 104-4

Title II of the Unfunded Mandates Reform Act of 1995 (UMRA), Public Law 104-4, establishes requirements for Federal agencies to assess the effects of their regulatory actions on State, local, and tribal governments and the private sector. Under section 202 of the UMRA, the Food and Nutrition Service generally must prepare a written statement, including a cost-benefit analysis, for proposed and final rules with "Federal mandates" that may result in expenditures to State, local, or tribal governments, in the aggregate, or to the private sector, of \$100 million or

more in any one year. When such a statement is needed for a rule, section 205 of the UMRA generally requires the Food and Nutrition Service to identify and consider a reasonable number of regulatory alternatives and adopt the least costly, more cost-effective or least burdensome alternative that achieves the objectives of the rule.

This rule contains no Federal mandates (under the regulatory provisions of Title II of the UMRA) for State, local, and tribal governments or the private sector of \$100 million or more in any one year. Thus, this rule is not subject to the requirements of sections 202 and 205 of the UMRA.

##### Executive Order 12372

The program addressed in this action is listed in the Catalog of Federal Domestic Assistance under No. 10.550, and is subject to the provisions of Executive Order 12372, which requires intergovernmental consultation with State and local officials (7 CFR part 3015, subpart V, and final rule-related notices published at 48 FR 29114, June 24, 1983, and 49 FR 22676, May 31, 1984).

##### Regulatory Flexibility Act

This rule has been reviewed with regard to the requirements of the Regulatory Flexibility Act of 1980 (5 U.S.C. 601-612). The Acting Administrator of the Food and Nutrition Service has certified that this action will not have a significant impact on a substantial number of small entities. State agencies, school food authorities and schools choosing to utilize this new method of inventory control will be affected. However, the majority of entities participating in the Food Distribution Programs will not be affected.

##### Executive Order 12988

This proposed rule has been reviewed under Executive Order 12988, Civil Justice Reform. The rule is intended to have preemptive effect with respect to any State or local laws, regulations or policies which conflict with its provisions or which would otherwise impede its full implementation. This rule is not intended to have retroactive effect. There are no administrative procedures that must be exhausted prior to any judicial challenge to the provisions of this rule or the applications of its provisions.

### Paperwork Reduction Act

Information collection requirements associated with the commodity processing program are approved under 0584-0293. This rule deletes the requirement for schools to maintain a dual inventory control system. Although the current inventory control requirements represent a burden on schools, estimated at 1.8 million hours annually for recipient agencies, this burden was not identified to or approved by the Office of Management and Budget. Therefore, deleting the burden requires no change to 0584-0293.

Allowing the limited substitution of donated poultry with commercial poultry significantly streamlines the manufacturing process for processors and allows recipients to receive end products on a timely basis. However, this rule does not relieve the processor from any of the current reporting or record keeping requirements contained in the regulations. Therefore, no changes are required to the current burden hours shown in 0584-0293.

### Background

#### *Substitution Issues*

In February of 1996, the Department of Agriculture announced a demonstration project to study the effects of allowing the substitution of commercial chicken for USDA donated chicken in the State processing program (61 FR 5373, Feb. 12, 1996). In the State processing program, pursuant to regulations in 7 CFR part 250, surplus commodities are made available by the Federal government to processors. Under State processing and inspection requirements at least comparable to those mandated by Federal agencies responsible for food purity and safety, the commodities are processed into food products intended for sale to school food authorities for consumption by students in the various school meal programs administered by the Food and Nutrition Service. The State processing program is authorized under section 14 of the Richard B. Russell National School Lunch Act, 42 U.S.C. 1762a.

In May of 1997 the project was expanded to include turkey as well as chicken. (62 FR 25885, May 12, 1997.) Only bulk pack poultry and poultry parts could be substituted under the project because the processing of these items could be more readily evaluated. The Department has determined from this demonstration project that current regulations regarding the non-substitution, non-diversion of poultry products has created onerous tracking and segregation requirements for both

processors and recipients. Allowing the substitution of donated poultry on this limited basis has resulted in more flexibility to processors to manage inventory and production schedules and has allowed processors to better service their customers, recipient agencies. Processors are now able to deliver end products in smaller quantities, as the customers prefer. This results in a substantial saving for the recipient agencies in storage and handling costs of the finished end product. The Department has determined that this substitution demonstration project has resulted in increased processor participation and provided a greater variety of processed end products to recipient agencies.

Therefore, the Department is proposing to change the regulations at 7 CFR 250.30(f) (hereinafter all references to regulations in this rulemaking are to regulations in Title 7 of the Code of Federal Regulations) to allow the substitution of commercial bulk pack poultry and poultry parts for USDA donated bulk pack poultry and poultry parts on a permanent basis. The ability for the processor to substitute is an option, not a requirement. Any substitution of poultry or poultry parts must be consistent with the "Buy American" provisions of Section 104(d) of Public Law 105-336 (The William F. Goodling Child Nutrition Reauthorization Act of 1998), which amended section 12 of the NSLA, 42 U.S.C. 1760(n). The "Buy American" provisions are in Program regulations at 7 CFR 210.21(d) for the National School Lunch Program and 7 CFR 220.16(d) for the School Breakfast Program and are discussed fully in a final rule titled "School Nutrition Programs: Nondiscretionary Technical Amendments" published on September 20, 1999 in the **Federal Register** at Volume 64 beginning on page 50735.

Currently, the substitution demonstration requires a processor to submit a substitution plan to the Department annually. Processors will still need to submit a final substitution plan to USDA for approval. Once approved, the plan will be permanent. However, any changes to the plan would require resubmission of the plan and approval by USDA before implementation. The prohibition against substituting backhauled poultry products will continue.

Substitution of donated fruits, vegetables, or eggs with commercial fruits, vegetables, or eggs is allowed under § 250.30(f)(4) of the current regulations with the written approval of FNS. Independent CPA audits of the processors who have received the

approval to substitute have identified no substitution of inferior product. Therefore, FNS is proposing to amend the regulations to allow full substitution in the further processing of fruits, vegetables, and eggs. Any substitution of fruits, vegetables, or eggs must be consistent with the "Buy American" provisions discussed above and subject to a 100% yield requirement. The Department believes that by making the substitution option permanent, processors will have more flexibility to properly service their customers. Substitution of donated commodity with commercial product of equal or better quality to the donated commodity will remain an option for processors.

#### *Commercial Labeling Issues*

Over the last year, USDA has conducted a demonstration project that allows vendors to use commercial labels rather than requiring USDA labels on foods made with or of USDA donated commodities used in the school meal programs. This project has demonstrated excellent benefits for recipient agencies including reduced delivery delays, increased competition, and reduced program costs. In addition, the project has helped eliminate a perceived stigma implied by the "generic" USDA labels.

However, using commercial labels has made it difficult for schools to distinguish between donated commodities and commercially purchased items in order to comply with current regulations to store and inventory donated commodities separately. These Federal requirements for storage and inventory of donated commodities have always been more stringent than the Federal requirements for foods that have been purchased using Federal reimbursement dollars from the National School Lunch Program. Schools currently must use generally accepted inventory and business management practices in order to safeguard commercially purchased products and maintain the financial integrity of their child nutrition program. For these reasons, the Department has determined that separate requirements for storage and inventory of commodities in the general food distribution regulations are redundant and more onerous than necessary to safeguard the value of commodities received at the school level. Therefore, the Department is proposing to amend the regulations at § 250.13(a) to define commodity value for the purpose of OMB Circular A-133, and at § 250.14(b), § 250.14(e), and § 250.14(f)(1) and (f)(2) to remove the requirement that "recipient agencies"

store and inventory USDA donated food separately. A technical amendment will be made in § 250.14(c) to correct sentence structure. Section 250.14(e) will be revised to reduce physical inventory requirements for schools in this section. To satisfy the requirements of OMB Circular A-133 for the purpose of valuing the commodities, both received and used by a recipient agency, guidance will be provided by the Food Distribution Division after publication of the final rule. State and commercial warehouses, and sub-distributing agencies continue to be required to store and inventory donated commodities separately.

**List of Subjects in 7 CFR Part 250**

Administrative practice and procedure, Food assistance programs, Grant programs, Social programs, Indians, Reporting and record keeping requirements, Surplus agricultural commodities.

Accordingly, 7 CFR Part 250 is amended as follows:

**PART 250—DONATION OF FOODS FOR USE IN THE UNITED STATES, ITS TERRITORIES AND POSSESSIONS AND AREAS UNDER ITS JURISDICTION**

1. The authority citation for Part 250 continues to read as follows:

**Authority:** 5 U.S.C. 301; 7 U.S.C. 612c, 612c note, 1431, 1431b, 1431e, 1431 note, 1446a-1, 1859, 2014, 2025; 15 U.S.C. 713c; 22 U.S.C. 1922; 42 U.S.C. 1751, 1755, 1758, 1760, 1761, 1762a, 1766, 3030a, 5179, 5180.

2. In § 250.13 add a new sentence at the end of paragraph (a)(5) to read as follows:

**§ 250.13 Distribution and control of donated foods.**

(a) \* \* \*  
 (5) \* \* \* To satisfy the requirement of OMB Circular Number A-133 for the purposes of valuing commodities, both received and used by a recipient agency, guidance will be provided as needed by the Food Distribution Division. (For availability for OMB Circulars referenced in the paragraph, see 5 CFR 1310.3.)

3. In § 250.14:
- a. Remove the word “Stock” at the beginning of paragraph (b)(4) and add in its place the words “Excepting recipient agencies, stock” ;
  - b. Remove the word “Conduct” from the beginning of the third sentence in paragraph (c) and add in its place the word “conduct” and remove the period at the end of the second sentence;
  - c. Revise paragraph (e);
  - d. Remove the words “or recipient agency’s” in paragraph (f)(1)

introductory text and add in its place the word “agency’s; and  
 e. Remove the words “and recipient agencies” in the second sentence of paragraph (f)(2).

The revision reads as follows:

**§ 250.14 Warehousing, distributing, and storage of donated foods.**

\* \* \* \* \*  
 (e) *Physical inventory.* During the annual review required by paragraph (c) of this section, distributing agencies and subdistributing agencies shall take a physical inventory of their storage facilities. The physical inventory shall be reconciled with each storage facility’s book inventory. The reconciliation records shall be maintained by the agency that contracted for or maintained the storage facility. Food items, which have been lost, stolen, or found to be out of condition, shall be identified and recorded. Potential excessive inventory, as described in paragraph (f) of this section, shall be reported by the subdistributing agency to the distributing agency. Corrective action on each deficiency noted during these inventories shall be initiated immediately and a written report of those corrective actions shall be forwarded to the distributing agency. Where applicable, the distributing agency shall pursue claims in accordance with § 250.15(c).

\* \* \* \* \*  
 4. In § 250.16, revise paragraph (a)(2) to read as follows:

**§ 250.16 Maintenance of records.**

(a) \* \* \*  
 (2) Distributing agencies shall require all subdistributing agencies to maintain accurate and complete records with respect to the receipt, distribution/ disposal, and inventory of donated foods, including end products processed from donated foods. Subdistributing agencies and recipient agencies must document any funds that arise from the operation of the distribution program, including refunds made to recipient agencies by a processor in accordance with § 250.30(k). Further, these documents should allow an independent determination of the specific accounts that benefit from these funds.

\* \* \* \* \*  
 5. In § 250.23, add a new paragraph (a)(3) to read as follows:

**§ 250.23 Buy American.**

(a) \* \* \*  
 (3) All food purchases must be consistent with the “Buy American” provision of Public Law 105-336 (The

William F. Goodling Child Nutrition Reauthorization Act of 1998).

\* \* \* \* \*

6. In § 250.30:
- a. Revise paragraph (f)(1) introductory text;
  - b. Remove paragraph (f)(1)(i) and redesignate paragraphs (f)(1)(ii) and (f)(1)(iii) as paragraphs (f)(1)(i) and (f)(1)(ii);
  - c. Revise newly redesignated paragraph (f)(1)(i);
  - d. Remove the words “specifically listed in paragraph (f)(1)(i) of this section” in the second sentence of paragraph (f)(2);
  - e. Remove paragraph (f)(4) and redesignate paragraph (f)(5) as paragraph (f)(4); and
  - f. Amend paragraph (g) by adding a sentence after the second sentence.

The revisions and additions read as follows:

**§ 250.30 State processing of donated foods.**

\* \* \* \* \*

(f) \* \* \*  
 (1) The processing contract may provide for substitution of donated foods as defined in § 250.3 except that donated beef and donated pork may not be substitutable. Any poultry processors that wish to substitute poultry must have a plan approved by USDA. No backhauled poultry product may be substitutable.

(i) All components of commercial foods substituted for any donated food must be identical or superior in every particular of the donated food specification. Records must be maintained to allow independent verification that the substituted food met the above condition.

\* \* \* \* \*

(g) \* \* \* As with the processing of donated poultry into end products, AMS graders must monitor the processing of any substituted commercial poultry to ensure that program integrity is maintained. \* \* \*

\* \* \* \* \*

Dated: February 14, 2002.  
**George A. Braley,**  
*Acting Administrator, Food and Nutrition Service.*  
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