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**DEPARTMENT OF AGRICULTURE**

**Food and Nutrition Service**

**7 CFR Part 250**

**[FNS-2017-0001]**

**RIN 0584-AE38**

**Revisions and Clarifications in Requirements for the Processing of Donated Foods**

**AGENCY:** Food and Nutrition Service (FNS), USDA

**ACTION:** Final rule.

**SUMMARY:** This rule revises and clarifies requirements for the processing of donated foods in order to: incorporate successful processing options tested in demonstration projects into the regulations, ensure accountability for donated foods provided for processing, increase program efficiency and integrity, and support vendor and State operability. The rule requires multi-State processors to enter into National Processing Agreements to process donated foods into end products, permits processors to substitute commercially purchased beef and pork of U.S. origin and of equal or better quality for donated beef and pork, and streamlines and modernizes oversight of inventories of donated foods at processors. The rule also revises regulatory provisions in plain language, to make them easier to read and understand.

**DATES:** This rule is effective [INSERT 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER].

**FOR FURTHER INFORMATION CONTACT:** Kiley Larson or Erica Antonson at Food Distribution Division, Food and Nutrition Service, 3101 Park Center Drive, Room 506, Alexandria, Virginia 22302, or by telephone (703) 305-2680.

**SUPPLEMENTARY INFORMATION:**

**I. Background and Description of Comments Received**

In a proposed rule published in the Federal Register on January 5, 2017 (82 FR 1231), Food Nutrition Service (FNS) proposed to amend Food Distribution regulations at 7 CFR part 250 to revise and clarify requirements for the processing of donated foods, in order to formalize processing options already being used in current practice, incorporate input received from processors and State and local agencies administering child nutrition programs, and rewrite much of 7 CFR part 250 Subpart C in a more user-friendly, “plain language” format. The Department of Agriculture (the Department or USDA) provides donated foods to State distributing agencies for distribution to recipient agencies (e.g., school food authorities) participating in the National School Lunch Program (NSLP) and other child nutrition or food distribution programs. In accordance with Federal regulations in 7 CFR part 250, distributing agencies may provide the donated foods to commercial processors for processing into end products for use in NSLP or other food programs.

For example, a whole chicken or chicken parts may be processed into precooked grilled chicken strips for use in NSLP. The ability to divert donated foods for further processing provides recipient agencies with more options for using donated foods in their programs. Program regulations ensure that State and recipient agencies, and program recipients, receive the full benefit of the donated foods provided to such processors for processing into end products.

FNS solicited comments through April 5, 2017, on the provisions of the proposed rulemaking. These comments are discussed below and are available for review at [www.regulations.gov](http://www.regulations.gov). To view the comments received, enter “FNS-2017-0001” in the search field on the main page of [www.regulations.gov](http://www.regulations.gov). Then click on “Search.” Under “Document Type”, select “Public Submission”.

FNS received 31 written comments regarding the proposed provisions from three associations and advocacy groups, eight State agencies, one recipient agency, thirteen private companies, and six individuals who did not identify an affiliation with an organization. Twelve of the comments received were duplicates of the comment submission from the American Commodity Distribution Association (ACDA). Two comments were supportive of the rule as proposed, in its entirety. The majority of the comments were supportive but recommended changes to add clarity and consistency to the language in the regulations.

Some commenters were supportive of the rule but opposed to a specific provision. There were no comments in opposition of the proposed rule as a whole.

Most commenters in support of the proposed rule indicated they were in favor of the clarifying changes and the consolidation of requirements previously tested in demonstration projects. Commenters also supported measures in the proposed rule to reduce administrative and reporting burdens on State distributing agencies and to streamline participation for industry stakeholders processing USDA Donated Foods.

Most commenters requested further clarification and guidance on the proposed rule and the provisions being changed. Specifically, commenters requested clarification on:

- The terminology used in the rule to ensure clear understanding of the intent and meaning of proposed provisions and requests to include commonly-used industry terms;
- The roles and responsibilities of FNS, State distributing agency, recipient agency, processor, and distributor staff in implementing some of the proposed provisions;
- The rationale behind some of the proposed provisions, including the allowable duration of some agreements required in the proposed rule;
- Whether certain entities, such as commercial entities using USDA Donated Foods in the preparation of meals, are designated as processors under the proposed rule;

- The process by which FNS establishes and disseminates the replacement value for USDA Donated Foods; and
- The method of oversight and enforcement that would be used for some of the proposed provisions including the proposed requirement for processors and distributors to enter into agreements with each other and the proposed requirement for any credit for the sale of by-products to be passed through to the recipient agency.

Commenters also requested that USDA:

- Collect, review, and file the agreements between processors and distributors required by the proposed rule;
- Include a provision in the final rule prohibiting distributors from acting as authorized agents of recipient agencies;
- Remove the provision in the proposed rule that discourages the pooling of inventory at distributors acting as the authorized agent of recipient agencies and instead establish a requirement for each distributor to enter into an agreement with FNS that 1) outlines distributor requirements, 2) transfers title of USDA Donated Foods to distributors when foods are in their possession, and 3) requires distributors to submit a surety bond to FNS to protect the value of USDA Donated Foods in their possession; and

- Include a provision in the final rule establishing the required method of calculation of inventory levels at processors and reducing the number of months used in the calculation from 12 to 10. This calculation, including the number of months used, is currently described in a Policy Memorandum.

## **II. Analysis of Comments Received and Regulatory Revisions, 7 CFR Part 250**

### **A. Definitions, § 250.2**

In § 250.2 we proposed to remove, revise, and add definitions relating to processing of donated foods. We proposed to remove the definitions of “Contracting agency” and “Fee-for-service.” We proposed to replace the term “Contracting agency” throughout the regulation with the specific agency (i.e., distributing and/or recipient agency) that may enter into a processing agreement. The meaning of the term “Fee-for-service” is clear in the context of the proposed regulatory provisions and no longer requires a separate definition. No comments were received on these proposed definition removals. Thus, the proposed removals are retained without change in this final rule.

We proposed to add definitions of “Backhauling,” “Commingling,” “End product data schedule,” “In-State Processing Agreement,” “National Processing Agreement,” “Recipient Agency Processing Agreement,” “Replacement value,” and “State Participation Agreement.” The definition of “Backhauling” would describe a means of delivery of donated food to a processor from a recipient agency’s storage facility.

The definition of “Commingling” would describe the common storage of donated foods with commercially purchased foods.

The definition of “End product data schedule” would convey the important function of this document in describing the processing of donated foods into finished end products. The definitions of “National Processing Agreement,” “Recipient Agency Processing Agreement,” “State Participation Agreement,” and “In-State Processing Agreement” would help the reader understand the different types of processing agreements permitted. These processing agreements are further described in § 250.30 of this final rule. No comments were received on these proposed definition additions. Thus, the proposed definitions are retained without change in this final rule.

The definition of “Replacement value” would clarify the donated food value that must be used by processors to ensure compensation for donated foods lost in processing or other activities. The definition of “Replacement value” reflects the price in the market at the time that the Department assigns the value whereas the definition of “Contract value” in current regulations reflects the Department’s current acquisition price, which is set annually. One commenter requested that the definition be amended to include any justifications that may be used to determine when the values will be changed and the method USDA would use to disseminate changed values. Replacement value is only changed by the Department in rare cases and only under special circumstances.

Under these special circumstances, the need to adjust the replacement value is determined on a case-by-case basis through consultation with the relevant State and local agencies. Changes are communicated directly to State and local agencies and the justifications for changes will vary significantly from case to case. Thus, the proposed definition is retained without change in this final rule.

B. Delivery and receipt of donated food shipments, § 250.11

In § 250.11(e), we proposed to describe the timing of transfer of title to donated foods and the agency to which title is transferred, in accordance with the amendments made by Section 4104 of the Agricultural Act of 2014 (P.L. 113-79) to Section 17 of the Commodity Distribution Reform Act and WIC Amendments of 1987, 7 U.S.C. 612c note, and the requirements under National Processing Agreements in this rule. In § 250.11(e) we proposed that the title to donated foods provided to a multi-State processor, in accordance with its National Processing Agreement, transfers to the distributing or recipient agency, as appropriate, upon the acceptance of finished end products at the time and place of delivery. No comments were received on this proposed change. Thus, the proposed language is retained without change in this final rule.

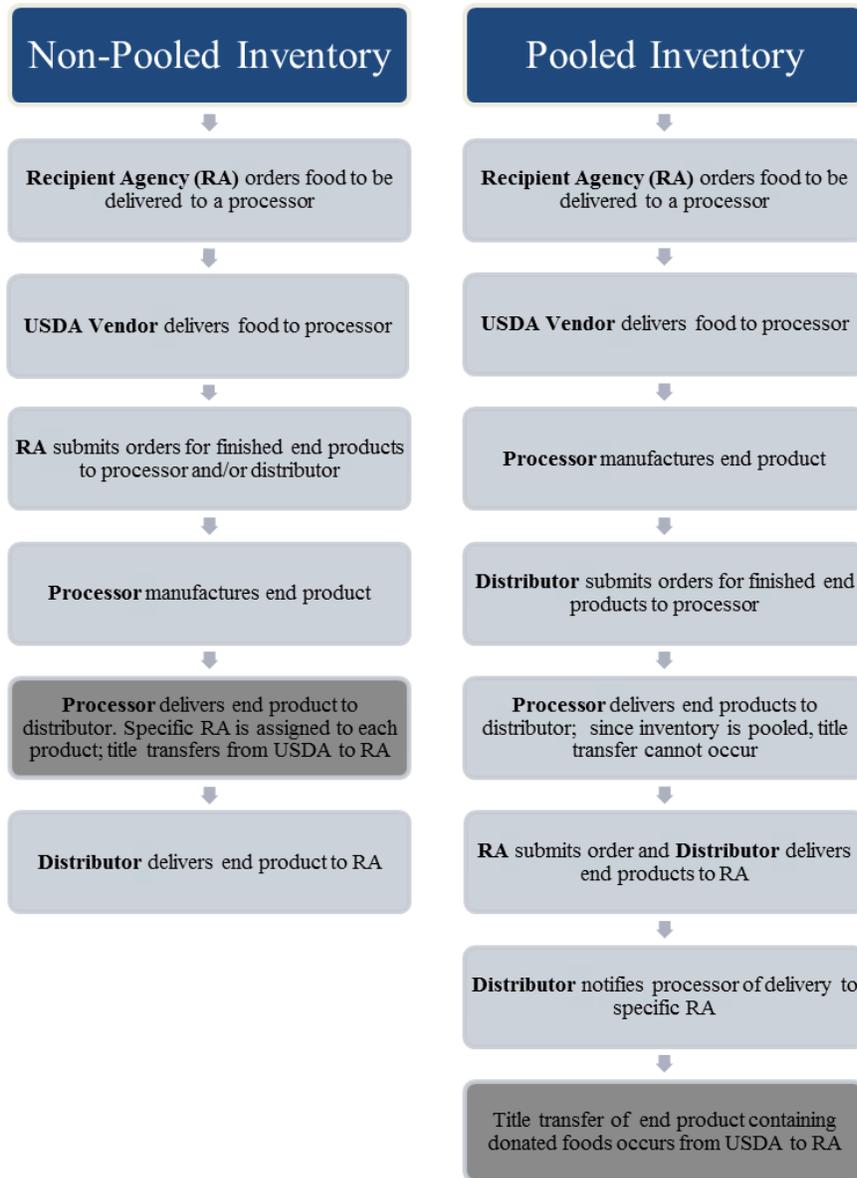
In § 250.11(e), we also proposed to require that when a distributor is contracted by the recipient agency for the transportation and/or storage of finished end products and is acting as the recipient agency's authorized agent (i.e., purchasing processed end products containing donated foods on behalf of the recipient agency),

title of donated foods would transfer to the recipient agency upon the acceptance of finished end products at the time and place of delivery at the recipient agency, or the distributor acting as the authorized agent of the recipient agency, whichever happens first. Many recipient agencies receiving finished end products from multi-State processors contract with a distributor to store end products and/or transport the finished end products to their facilities. The inclusion of distributors in the supply chain for finished end products creates challenges related to tracking and reporting the value of donated foods. Because processors are not a party to the contractual relationship between recipient agencies and distributors, processors lose control of finished end products once they are delivered to the distributors designated by each recipient agency. Pursuant to current regulations, however, processors are required to maintain a bond for the value of those finished end products.

As a result, in situations where recipient agencies contract with a distributor to store and/or transport processed end products containing donated foods and act as their authorized agent, complications can arise that may impede the transfer of title described above. Some processors and distributors, working in this manner, manufacture and/or order some processed end products prior to receiving donated food orders from recipient agencies. This is sometimes termed “inventory pooling” (as illustrated below). Under current regulations, title cannot transfer to the recipient agency at the time of delivery at its contracted distributor because neither the processor nor the distributor know which recipient agency will receive which products.

The intent of § 250.11(e) is to discourage the pooling of processed end products.

Current Practice:



Many comments were received on this provision ranging from overall support to overall opposition. One commenter expressed strong support for the provision, claiming that it would increase efficiency and program integrity.

One commenter expressed support for the provision but requested clarification that title for donated foods will never transfer to the distributor but will only transfer from USDA to the recipient agency. Thirteen commenters expressed understanding of the Department's position to include the provision but requested clarifying language be included to instruct processors to closely monitor distributor transactions and reporting practices, and to label the practice as it is known, inventory pooling.

In response, we would point out that processors should always closely monitor distributor transactions and reporting practices to ensure that all parties are adhering to the requirements of 7 CFR part 250 and the processor's processing agreement. Transaction monitoring and reporting maybe outlined in the agreement between the distributor and processor required in § 250.30(i). Inventory pooling, in this context, refers to a practice employed by distributors. § 250.11(e) is focused on clarifying when title transfers, ensuring that processors know which School Food Authority (SFA) is accepting ownership of end products. Therefore, the term "pooling" is not referenced in the regulatory text.

One commenter acknowledged the challenges that the practice of inventory pooling creates for entities within the end product supply chain but suggested alternate methods for addressing them. The alternate methods suggested were prohibiting distributors from acting as authorized agents of SFAs and requiring that distributors enter into agreements with FNS to furnish a surety bond for donated foods in their inventory or transfers title to donated foods to distributors while in their inventory. Current statutory provisions do not permit the transfer of title of donated foods to a distributor or a requirement for a distributor to furnish

a surety bond to USDA. In addition, a regulatory change of this magnitude must be subject to public review and comment prior to being codified. Therefore, FNS is not able to implement these alternatives at this time.

Two commenters expressed strong opposition to the provision. The commenters felt that inventory pooling provided flexibility for distributors and allowed them to more easily serve recipient agencies. Similar to other commenters on this provision, the commenters felt that an alternative could be to require distributors to enter into agreements with FNS to furnish a surety bond for donated foods in their inventory. For the reasons described in the previous paragraph, this proposed alternative cannot be implemented at this time. The commenters also expressed concerns about the administrative burden associated with maintaining separate school-owned inventories for each eligible recipient agency, including individual stock keeping units (SKUs) for each end product and recipient agency. This interpretation of the intent of this provision is incorrect. FNS does not expect distributors to maintain separate physical inventories for every eligible recipient agency as the commenters describe. Doing so would be overly burdensome and would contradict the long-established concept of substitution in USDA Foods processing. However, FNS understands that this provision may require further guidance and that there may be potential benefits of establishing a different accountability mechanism for processed end products at distributors through agreements or other mechanisms. FNS will explore whether potential pilot projects could be used to test these approaches. The proposed provision is retained without change in this final rule.

C. Reporting requirements, § 250.18

In § 250.18(b) we proposed to retain the requirement for processors to submit monthly performance reports to the distributing agency. However, we proposed to replace the reference to § 250.30(m) with § 250.37(a) as the section is being re-designated and revised. No comments were received on this proposed change. Thus, the proposed language is retained without change in this final rule.

D. Recordkeeping requirements, § 250.19

In § 250.19(a) we proposed to amend the recordkeeping requirements for processors and instead reference specific recordkeeping requirements for processors contained in Subpart C. No comments were received on this proposed change. Thus, the proposed language is retained without change in this final rule.

E. Subpart C—Processing of Donated Foods

FNS proposed to completely revise current Subpart C of 7 CFR part 250 to more clearly present the specific processing requirements and rewrite these sections in plain language. We proposed to include the requirements for specific processing activities in the order in which they most commonly occur; i.e., entering into processing agreements, processing of donated foods into end products, sale of end products, submission of reports, etc. We also proposed to change the heading of Subpart C to Processing of Donated Foods. Comments received on this Subpart are outlined below. The new sections proposed under the revised Subpart C include the following:

250.30 Processing of donated foods into end products.

250.31 Procurement requirements.

250.32 Protection of donated food value.

250.33 Ensuring processing yields of donated foods.

250.34 Substitution of donated foods.

250.35 Storage, food safety, quality control, and inventory management.

250.36 End product sales and crediting for the value of donated foods.

250.37 Reports, records, and reviews of processor performance.

250.38 Provisions of agreements.

250.39 Miscellaneous provisions.

1. Processing of donated foods into end products, § 250.30

In § 250.30, we proposed to state clearly why donated foods are provided to processors for processing, and we proposed to describe the different types of processing agreements permitted, including National, In-State, and Recipient Agency Processing Agreements. However, we proposed to include the specific provisions required for each type of agreement in § 250.38, as the reason for their inclusion would only be clear with an understanding of the processing requirements contained in the preceding sections.

In § 250.30(a), we proposed to describe the benefit of providing donated foods to a processor for processing into end products, and we proposed to clarify that a processor's use of a commercial facility to repackage donated foods, or to use donated foods in the preparation of meals, is also considered processing in 7 CFR part 250. Two commenters requested that this provision be amended to clarify that repackaging of USDA Donated Foods in meals that are vended to a school food authority is subject to the processing

requirements in 7 CFR part 250. To clarify our intent in this final rule, the words “A processor’s” are deleted from the last sentence of § 250.30(a) to indicate that any commercial entity’s use of a commercial facility to repackage donated foods, or to use donated foods in the preparation of meals, is also considered processing in 7 CFR part 250.

Two commenters expressed concerns that considering meal vendors as processors under 7 CFR part 250 could impact competition and limit the use of USDA Donated Foods at recipient agencies contracted with meal vendors. The commenters requested that meal vendors be permitted to operate in a similar manner as Food Service Management Companies which must receive USDA Donated Foods and prepare meals at the recipient agency’s facility. Meal vendors have long been considered processors under current regulations. The final rule is only clarifying an already established requirement. Thus, the proposed provision is retained without change in this final rule. We also want to clarify that SFAs providing meals containing USDA Donated Foods to another recipient agency under an intergovernmental agreement are not considered processors in this part.

In § 250.30(b), we proposed to clarify that processing of donated foods must be performed in accordance with an agreement between the processor and FNS, between the processor and the distributing agency, or, if permitted by the distributing agency, between the processor and a recipient agency (or subdistributing agency). We proposed to include in § 250.30(b) the stipulation in current § 250.30(c)(5)(ix) that an agreement may not obligate the distributing or recipient agency, or FNS, to provide donated foods to a processor for processing. We proposed to clarify that the agreements described in this section are

required in addition to, not in lieu of, competitively procured contracts required in accordance with § 250.31. We proposed to revise the requirement in current § 250.30(c)(4) that indicates which official of the processor must sign the processing agreement and more simply state in proposed § 250.30(b) that the processing agreement must be signed by an authorized individual acting for the processor. We proposed to remove the stipulation in current § 250.30(c)(1) that a processing agreement must be in standard written form. No comments were received on the proposed changes in this subsection. Thus, the proposed provision is retained without change in this final rule.

In § 250.30(c), we proposed to require that a multi-State processor enter into a National Processing Agreement with FNS to process donated foods into end products, in accordance with end product data schedules approved by FNS. We also indicated that, in the proposed § 250.32, FNS holds and manages the multi-State processor's performance bond or letter of credit to protect the value of donated food inventories under the National Processing Agreement. We indicated that FNS does not itself procure or purchase end products under such agreements, and that a multi-State processor must enter into a State Participation Agreement with the distributing agency in order to sell nationally approved end products in the State, as in the proposed § 250.30(d). No comments were received on the proposed changes in this subsection. Thus, the proposed provision is retained without change in this final rule.

In § 250.30(d), we proposed to require the distributing agency to enter into a State Participation Agreement with a multi-State processor to permit the sale of end products

produced under the processor's National Processing Agreement in the State, as previously indicated. The State Participation Agreement is currently utilized in conjunction with National Processing Agreements in the demonstration project. Under the State Participation Agreement, we proposed to permit the distributing agency to select the processor's nationally approved end products for sale to eligible recipient agencies within the State or to directly purchase such end products. The processor may provide a list of such nationally approved end products in a summary end product data schedule. We also proposed to permit the distributing agency to include other processing requirements in the State Participation Agreement, such as the specific methods of end product sales permitted in the State, in accordance with the proposed § 250.36, (e.g., a refund, discount, or indirect discount method of sales), or the use of labels attesting to fulfillment of meal pattern requirements in child nutrition programs. We proposed to require the distributing agency to utilize selection criteria in current § 250.30(c)(1) to select processors with which to enter into State Participation Agreements. No comments were received on State Participation Agreements overall.

However, one commenter requested that "the marketability or acceptability of end products" be removed from the list of selection criteria that State agencies must evaluate prior to entering into State Participation Agreements with multi-State processors. The commenter felt that the requirement was burdensome and impractical for large States. Marketability and acceptability are important factors for end products served in child nutrition programs to ensure that products are well-suited to the local market and promote the use of donated foods. The requirement to include marketability and acceptability as selection criteria is

long standing, and State agencies have discretion in how they evaluate products under these criteria. Thus, the proposed provision is retained without change in this final rule.

In § 250.30(e), we proposed to clarify the distinction between master agreements and other In-State Processing Agreements and to include in this proposed section the required criteria in current § 250.30(c)(1) for distributing agencies that procure end products on behalf of recipient agencies or that limit recipient agencies' access to the procurement of specific end products through its master agreements. We proposed to require that the distributing agency enter into an In-State Processing Agreement with an in-State processor (i.e., a processor which only services recipient agencies in a single State via a production facility located in the same State) to process donated foods, as currently required under the demonstration project. Under all In-State Processing Agreements, the distributing agency must approve end product data schedules submitted by the processor, hold and manage the processor's performance bond or letter of credit, and assure compliance with all processing requirements.

No comments were received on In-State Processing Agreements overall, however one commenter requested that marketability and acceptability be removed from the list selection criteria that State agencies must evaluate prior to entering into an In-State Processing Agreement with an in-State processor. As stated above, marketability and acceptability are important factors for end products served in child nutrition programs and the requirement to include them as a selection criteria is long standing. One commenter also requested that additional detail be included instructing State agencies on how to calculate bond and letter

of credit levels for in-State processors. As proposed, § 250.30(e), provides State agencies with the flexibility to set bond and letter of credit levels to reflect State laws and the status of their State's processing market. However, FNS recognizes that State agencies may benefit from further guidance and will explore whether policy guidance can be used to aid States on this matter. Thus, the proposed provision is retained without change in this final rule.

In § 250.30(f), we proposed to allow distributing agencies to permit recipient agencies (or subdistributing agencies) to enter into agreements with processors to process donated foods and to purchase the finished end products. These agreements are referred to as Recipient Agency Processing Agreements. We also proposed to clarify that, under such agreements, the distributing agency may also delegate oversight and monitoring to the recipient agency to approve end product data schedules or select nationally approved end product data schedules, review processor performance reports, manage the performance bond or letter of credit of an in-State processor, and monitor other processing activities. All such activities must be performed in accordance with the requirements of this part. We proposed to clarify that a recipient agency may also enter into a Recipient Agency Processing Agreement, and perform the activities described above, on behalf of other recipient agencies, in accordance with an agreement between the parties (such as in a school cooperative). We proposed to require the recipient agency to utilize selection criteria in current § 250.30(c)(1) to select processors with which to enter into Recipient Agency Processing Agreements. The distributing agency must approve all Recipient Agency Processing Agreements. No

comments were received on this proposed provision. Thus, the proposed language is retained without change in this final rule.

In § 250.30(g), we proposed to retain the requirement that distributing agencies must test end products with recipient agencies prior to entering into processing agreements, to ensure that they will be acceptable to recipient agencies. We proposed to clarify that the requirements only apply to distributing agencies that procure end products on behalf of recipient agencies or otherwise limit recipient agencies' access to the procurement of specific end products, and we proposed to clarify that the distributing agency may permit recipient agencies to test end products. We also proposed to amend the current requirement that the distributing agency develop a system to monitor product acceptability on a periodic basis by requiring instead that the distributing agency, or its recipient agencies, must monitor product acceptability on an ongoing basis. No comments were received on this proposed provision. Thus, the proposed language is retained without change in this final rule.

In § 250.30(h), we proposed that a processor may not assign any processing activities under its processing agreement, or subcontract with another entity to perform any aspect of processing, without the written consent of the other party to the agreement, which may be the distributing, subdistributing, or recipient agency, or FNS. We proposed to permit the distributing agency to provide the required written consent as part of its State Participation Agreement or In-State Processing Agreement with the processor. One commenter requested that we require distributing agencies to approve of subcontractors in its State Participation

Agreement with the processor. The National Processing Agreement requires subcontractor agreements but States should have flexibility in how they provide written consent for subcontracting. Thus, the proposed language is retained without change in this final rule.

In § 250.30(i), we proposed to require agreements between processors and distributors. We proposed that the agreement, initiated by the processor before releasing finished end products to a distributor, must reference, at a minimum, the financial liability (i.e., who must pay) for the replacement value of donated foods, not less than monthly end product sales reporting frequency, requirements under § 250.11, and the applicable value pass through system to ensure that the value of donated foods and finished end products are properly credited to recipient agencies. We also proposed that distributing agencies could set additional requirements such as requiring that copies or templates of these agreements be included with the submission of signed State Participation Agreements. Many comments were received on this provision.

One commenter noted strong support for this provision overall, but requested that clarifying language be added to the provision to prescribe that financial liability for donated foods in the agreement is assigned to the party that caused a loss or negative balance to occur. These agreements are designed to allow processors and distributors to draft an agreement that mutually protects each of their interests, including financial liability. FNS will not be a party to these agreements and does not want to dictate, in regulations, the structure of specific provisions for all situations that the parties may encounter. Therefore, this language will not be included in the final rule. However, FNS will explore whether further policy

guidance on this matter is needed. The commenter also requested that provisions be added to specifically address distributors, including requiring written agreements between a distributor and FNS that covers liability, reporting, and delivery requirements. FNS does not maintain a direct relationship with distributors. Therefore, this language will not be included in the final rule.

Fourteen commenters noted support for the provision but requested that we add a requirement that agreements between processors and distributors must be submitted to FNS for review and record keeping. FNS will not be a party to these agreements and is not in a position to evaluate if individual agreements are appropriate. States will also not be required to review or collect these agreements. However, we agree with the importance of having an oversight mechanism in place to ensure that the agreements are in place as required. Verification of these agreements will be required as part of the audits that processors must obtain under current requirements at § 250.20(b). Moreover, requiring processors to submit these agreements to FNS for review and record keeping would impose an additional information collection burden. Such a provision would require a separate rule and would be subject to public comment. Therefore, this language will not be included in the final rule.

One commenter noted support for the provision but requested that agreements between processors and distributors be made permanent. Under the proposal, the duration of these agreements is up to the specific processor and distributor in the agreement. If both parties agree, the agreement could be permanent. Therefore, no change is being made in the final

rule. The commenter also requested that the required reporting frequency in the agreement be increased from the proposed “not less than monthly” to “not more than five calendar days.” The commenter felt that the more frequent reporting would improve coordination between the processor and distributor and allow the processor to be more timely with the monthly performance reports. Improvements in technology are allowing many distributors to report end product sales to processors much more frequently than monthly. This is a positive trend which FNS supports insofar as it should result in improved transparency and coordination. However, not all distributors are currently capable of meeting that requirement. Therefore, this language will not be included in the final rule.

Two commenters were opposed to requiring agreements between processors and distributors. One of these commenters noted that some of the required topics in the agreements, such as financial liability, reporting frequency, and value pass through method are already the responsibility of the processor via the National Processing Agreement or regulations and that that may diminish the usefulness of the agreements between processors and distributors. This commenter also stated a concern that State agencies may create additional burdensome requirements for these agreements that may discourage processor and distributor participation. The required topics are only intended to be a starting point. Processors and distributors may include additional provisions that more accurately reflect their interests or business model. State agencies must be able to add requirements to reflect State laws or the status of the market within their State. The second of these commenters requested that agreements between processors and distributors be encouraged as opposed to required. Requiring these agreements will ensure more communication, transparency, and

cooperation between processors and distributors. This provision was widely supported in other comments. Thus, the proposed language is retained without change in this final rule.

In § 250.30(j), we proposed to permit all agreements between a distributing, subdistributing, or recipient agency and a processor to be up to five years in duration, as opposed to the current one year limit with an option to extend for two additional years. This proposal would permit the appropriate agency to determine the length of agreement that would be to its best advantage, within the five-year limitation, and would reduce the time and labor burden imposed on such agencies. We proposed to make National Processing Agreements permanent. We proposed that amendments to any agreements may be made as needed (e.g. when new subcontractors are added), with the concurrence of the parties to the agreement, and that such amendments would be effective for the duration of the agreement, unless otherwise indicated.

One commenter requested that all agreements, including the State Participation, In-State Processing, and Recipient Agency Processing Agreements are made permanent. In-State and Recipient Agency Processing Agreements are sometimes subject to frequent updates and are often executed in conjunction with a procurement action. Therefore, the proposed five year duration limit is retained in this final rule for In-State and Recipient Agency Processing Agreements. However, State Participation Agreements are designed to allow State agencies to supplement requirements in the National Processing Agreement for multi-State processors. Therefore, the final rule is amended to allow State agencies to make their State Participation Agreements permanent. Amendments to State Participation Agreements

should still be made when needed, for example, to approve subcontractors arrangements or approve end products to be sold in the State.

We proposed to remove the following requirements or statements in current § 250.30 related to processing agreements, as they are overly restrictive or unnecessary given current practice and administrative structure:

- The requirement in current § 250.30(c)(1) that the FNS Regional Office review processing agreements.
- The requirement in current § 250.30(c)(3) that the agreement be prepared and reviewed by State legal staff to ensure conformance with Federal regulations.
- The requirement in current § 250.30(l) that the distributing agency provide a copy of the 7 CFR part 250 regulations to processors and a copy of agreements to processors and the FNS Regional Office.

No comments were received on these proposed removals. Thus, the proposed removals are retained without change in this final rule.

## 2. Procurement requirements, § 250.31

The requirements for the procurement of goods and services under Federal grants are established in 2 CFR part 200 and USDA implementing regulations at 2 CFR part 400 and part 416, as applicable. In § 250.31(a), we proposed to indicate the applicability of these requirements to the procurement of processed end products, distribution, or of other processing services related to donated foods. We also proposed that distributing or recipient agencies may use procurement procedures that conform to applicable State and local laws,

as appropriate, but must ensure compliance with the Federal procurement requirements. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.31(b), we proposed to require specific information in procurement documents, to assist recipient agencies in ensuring that they receive credit for the value of donated foods in finished end products. We proposed to require that procurement documents include the price to be charged for the finished end product or other processing service, the method of end product sales that would be utilized, an assurance that crediting for donated foods would be performed in accordance with the applicable requirements for such method of sales in proposed § 250.36, the contract value of the donated food in the finished end products, and the location for the delivery of the finished end products. We proposed to remove current requirements for the provision of pricing information outside of the procurement process, including:

- 1) The requirement in current § 250.30(c)(5)(ii) that pricing information be included with the end product data schedule; and
- 2) The requirements in current § 250.30(d)(3) and (e)(2) that the processor provide pricing information summaries to the distributing agency, and the distributing agency provide such information to recipient agencies, as soon as possible after completion of the agreement.

One commenter requested clarification on the applicability of these requirements to subsequent procurements conducted by a distributor acting as a recipient agency's

authorized agent. The information required in procurement documents in this provision apply to all procurements for end products containing donated foods, regardless of who performed the procurement. The commenter also requested clarification that the requirement to include the value of the donated food in the end products in procurement documents does not remove the requirement to include the value of the donated food in the end products on the end product data schedule. This reflects an incorrect understanding of current requirements. The value of donated foods is no longer required on end product data schedules. Including the value on the end product data schedule would require it to be revised with every change in value. However, FNS publishes summary end product data schedules which include the value of donated food for each end product. The summary end product data schedules can be used to confirm the accuracy of the value of donated food listed in the procurement documents. Thus, the proposed language is retained without change in this final rule.

### 3. Protection of donated food value, § 250.32

In § 250.32(a), we proposed to include the requirement that the processor obtain financial protection to protect the value of donated foods prior to their delivery for processing, by means of a performance bond or irrevocable letter of credit. We proposed to remove escrow accounts as an option for financial protection. Multi-State processors must provide the performance bond or irrevocable letter of credit to FNS, in accordance with its National Processing Agreement. We proposed to clarify that the amount of the performance bond or letter of credit must be sufficient to cover at least 75 percent of the value of donated foods in the processor's physical or book inventory, as determined annually, and at the discretion of

FNS, for processors under National Processing Agreements. For multi-State processors in their first year of participation in the processing program, the amount of the performance bond or letter of credit must be sufficient to cover 100 percent of the value of donated foods, as determined annually, and at the discretion of FNS. In-State processors must provide the performance bond or letter of credit to the distributing or recipient agency, in accordance with its In-State or Recipient Agency Processing Agreement. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.32(b), we proposed to indicate the conditions under which the distributing or recipient agency must call in the performance bond or letter of credit. We also proposed to indicate that FNS would call in the performance bond or letter of credit under the same conditions and would ensure that any monies recovered by FNS are reimbursed to distributing agencies for losses of entitlement foods. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

#### 4. Ensuring processing yields of donated foods, § 250.33

In § 250.33, we proposed to retain the required submission of the end product data schedule and to more specifically describe the required processing yields of donated food, which is currently referred to as the yield. In § 250.33(a), we proposed to require submission of the currently required information on the end product data schedule, with the exception of the price charged for the end product or other pricing information and the contract value of the donated food. As described above, in the proposed § 250.31, pricing information must be included in the procurement of end products or other processing services relating to donated

foods. Inclusion of such information on end product data schedules may be misleading, as it may lead some recipient agencies to conclude that a competitive procurement has been performed by the distributing agency under its In-State Processing Agreement or State Participation Agreement. Prices currently included on end product data schedules generally reflect the highest price that a processor would charge for the finished end product and not necessarily the actual price of the end product.

We also proposed to require inclusion of the processing yield of donated food, which may be expressed as the quantity of donated food (pounds) needed to produce a specific quantity of end product or as the percentage of donated food returned in the finished end product.

We proposed to retain the requirement that end product data schedules be approved by the distributing agency under In-State Processing Agreements. We proposed to clarify that the end product data schedules for products containing donated red meat or poultry must also be approved by the Department, as is currently required under program policy. We proposed to require that, under National Processing Agreements, end product data schedules be approved by the Department. Lastly, we proposed to clarify that an end product data schedule must be submitted in a standard electronic format dictated by FNS, and approved for each new end product that a processor wishes to provide or for a previously approved end product in which the ingredients or other pertinent information have been altered. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.33(b), we proposed to describe the different processing yields of donated foods that may be approved in end product data schedules. In an effort to simplify the yield requirements and streamline monitoring for distributing and recipient agencies we proposed to limit the processing yields to 100 percent yield, guaranteed yield, and standard yield. In § 250.33(b)(1), we proposed to include the current 100 percent yield requirement. We proposed to indicate that FNS may make exceptions to the 100 percent yield requirement, on a case-by-case basis. Exceptions to the 100 percent yield requirement can result in one of the alternate processing yields described below. Two commenters expressed support for the removal of guaranteed minimum yield. Thus, the proposed language is retained without change in this final rule.

In § 250.33(b)(2), we proposed to describe guaranteed yield. Under guaranteed yield, the processor must ensure that a specific quantity of end product would be produced from a specific quantity of donated food put into production. The guaranteed yield for a specific product is determined and agreed upon by the parties to the processing agreement, and, for In-State and Recipient Agency Processing Agreements, approved by the Department. Guaranteed yield is generally used when significant variance is present across processors in manufacturing and yield for a particular end product. The guaranteed yield must be indicated on the end product data schedule. One commenter requested clarification that a specific quantity of end product is tracked or reported as pounds of donated food per case of end product. This is correct. Thus, the final rule is amended to clarify.

In § 250.33(b)(3), we proposed to describe standard yield. Under standard yield, the processor must ensure that a specific quantity of end product, as determined by the Department, would be produced from a specific quantity of donated food. The standard yield is determined and applied uniformly by the Department to all processors for specific donated foods. The established standard yield is higher than the average yield under normal commercial production and serves to reward those processors that can process donated foods most efficiently. If necessary, the processor must use commercially purchased food of the same generic identity, of U.S. origin, and equal or better in all USDA procurement specifications than the donated food to provide the number of cases required to meet the standard yield to the distributing or recipient agency, as appropriate. The standard yield must be indicated on the end product data schedule. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.33(c), we proposed to require that the processor compensate the distributing or recipient agency, as appropriate, for the loss of donated foods, or for commercially purchased foods substituted for donated foods. Loss of donated foods may result for a number of reasons, including the processor's failure to meet the required processing yield or failure to produce end products that meet required specifications, spoilage or damage of donated foods in storage, or improper distribution of end products. In order to compensate for such losses of donated foods, we proposed to require that the processor:

- 1) Replace the lost donated food or commercial substitute with commercially purchased food of the same generic identity, of U.S. origin, and equal or better in all USDA procurement specifications than the donated food; or

- 2) Return end products that are wholesome but do not meet required specifications to production for processing into the requisite quantity of end products that meet the required specifications; or
- 3) Pay the distributing or recipient agency, as appropriate, for the replacement value of the donated food or commercial substitute only if the purchase of replacement foods is not feasible and the processor has received approval. In-State processors would be required to obtain distributing agency approval for such payment and multi-State processors would be required to obtain FNS approval.

No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.33(d), we proposed to retain the requirement that processors must credit the distributing or recipient agency, as appropriate, for the sale of any by-products resulting from the processing of donated foods or of commercially purchased foods substituted for donated foods. However, we proposed to require crediting through invoice reductions or another means of crediting. We also proposed to clarify that the processor must credit the appropriate agency for the net value received from the sale of by-products after subtraction of any documented expenses incurred in preparing the by-product for sale. We proposed to remove the requirement in current § 250.30(c)(5)(viii)(D) that the processor credit the distributing or recipient agency for the sale of donated food containers because the burden required to monitor the credit outweighed the value returned. One commenter requested clarification on the method of oversight to ensure that distributing or recipient agencies are credited for the sale of by-products by processors. Verification that appropriate credits for

the sale of by-products have occurred is required as part of the audits required of processors under current requirements at § 250.20(b). Thus, the proposed language is retained without change in this final rule.

In § 250.33(e), we proposed to retain the requirements that processors must meet applicable Federal labeling requirements, and must follow the procedures required for approval of labels for end products that claim to meet meal pattern requirements in child nutrition programs. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

#### 5. Substitution of donated foods, § 250.34

In § 250.34(a), we proposed to permit a processor to substitute any donated food that is delivered to it from a USDA vendor with commercially purchased food of the same generic identity, of U.S. origin, and of equal or better quality in all Departmental purchase specifications than the donated food. We proposed to clarify that commercially purchased beef, pork or poultry must meet the same specifications as donated product, including inspection, grading, testing, and humane handling standards, and must be approved by the Department in advance of substitution. We proposed to remove the required elements of a processor's plan for poultry substitution in current § 250.30(f)(1)(ii)(B). We also proposed to allow a processor the option to substitute any donated food in advance of the receipt of the donated food shipment and to more clearly describe the processor's assumption of risk should the Department be unable to purchase and deliver any donated food so substituted. Lastly, we proposed to require that commercially purchased food substituted for donated

food meet the same processing yield requirements that would be required for the donated food, as in the proposed § 250.33. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.34(b), we proposed to prohibit substitution or commingling of all backhauled donated foods and to require that the processor, if amenable to reformulation, process such end products into end products for sale and delivery to the same recipient agency that provided them and not to any other recipient agency. In other words, the recipient agency which backhauls a previously processed end product to a processor for reformulation must in turn use the reformulated end products, containing their backhauled product, in their food service. Additionally, we proposed to prohibit the processor from providing payment to the recipient agency in lieu of processing and prohibit the distributing or recipient agency from transferring the backhauled food to another processor. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.34(c), we proposed to retain current requirements at § 250.30(g), which state that the processing of donated beef, pork and poultry must occur under Federal Quality Assessment Division grading in order to assure that substitution and yield requirements are met and that end products conform with the applicable end product data schedule. The Department's Agricultural Marketing Service conducts such grading. The processor is responsible for paying the cost of the acceptance service grading. The processor must maintain records (including grading certificates) necessary to document that substitution of all donated foods has been conducted in accordance with the requirements in 7 CFR part

250. One commenter expressed that the financial burden of grading can be overwhelming for small processors. FNS recognizes that the cost of grading requirements is not insignificant to small processors. However, grading requirements are important for ensuring that Federal regulations are adhered to. Further, small processors are typically in-State processors and not multi-State processors and, when circumstances warrant it, State distributing agencies can waive grading requirements under In-State and Recipient Agency Processing Agreements, according to proposed § 250.34(d). Thus, the proposed language is retained without change in this final rule.

In § 250.34(d), we proposed to permit distributing agencies to approve a waiver of the grading requirement for donated beef, pork, or poultry under certain conditions. However, we proposed to indicate that such waivers may only be approved on a case by case basis—e.g., for a specific production run. The distributing agency may not approve a blanket waiver of the requirement. We also included the stipulation that a waiver may only be approved if the processor's past performance indicates that the quality of the end product would not be adversely affected. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.34(e), we proposed to include the current provision that the processor may use any substituted donated food in other processing activities conducted at its facilities. We proposed to remove the stipulation, in current § 250.30(f)(4), that title to the substituted donated food passes to the processor upon the initiation of processing of the end product with the commercial substitute. The transfer of title to donated foods, which are part of the

Federal grant, is limited to the distributing agency or recipient agency, as the recipients of the grant. Subsequent donated food activities may be performed in accordance with Federal regulations and the terms of processing agreements but would not include a further transfer of title. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

6. Storage, food safety, quality control, and inventory management, § 250.35

In § 250.35, we proposed to include requirements for the storage, food safety oversight, quality control, and inventory management of donated foods provided for processing. In § 250.35(a), we proposed to require the processor to ensure the safe and effective storage of donated foods, including compliance with the general storage requirements in current § 250.12, and to maintain an effective quality control system at its processing facilities. We proposed to require the processor to maintain documentation to verify the effectiveness of its quality control system and to provide such documentation upon request. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.35(b), we proposed to require that all processing of donated foods is conducted in compliance with all Federal, State, and local requirements relative to food safety. This represents a simplification of current regulations. One commenter requested that the Agricultural Marketing Service (AMS) be explicitly listed along with Federal, State, and local requirements. AMS is only one of many Federal agencies with pertinent requirements that would be included in this list and applicable requirements will vary from processor to

processor depending on the type of product produced, among other factors. Thus, the proposed language is retained without change in this final rule.

In § 250.35(c), we proposed to clarify that a processor may commingle donated foods and commercially purchased foods, unless the processing agreement specifically stipulates that the donated foods must be used in processing, and not substituted, or the donated foods have been backhauled from a recipient agency. However, such commingling must be performed in a manner that ensures the safe and efficient use of donated foods, as well as compliance with substitution requirements, and with reporting of donated food inventories on performance reports, as required in 7 CFR part 250.

We also proposed to require that processors ensure that commingling of finished end products with other food products by distributors results in the sale to recipient agencies of end products that meet substitution requirements. One way that this may be achieved is by affixing the applicable USDA certification stamp to the exterior shipping containers of such end products. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.35(d), we proposed to include the current limitation on inventories of donated foods at a processor and to clarify that distributing agencies are not permitted to submit food orders for processors reporting no sales activity during the prior year's contract period unless documentation is submitted by the processor which outlines specific plans for donated food drawdown, product promotion, or sales expansion. A processor may not have on hand more

than a six-month supply of donated foods, based on an average amount utilized for that period. However, the distributing agency may, at the processor's request, provide written approval to allow the processor to maintain a larger amount of donated foods in inventory if it determines that the processor may efficiently store and process such an amount. We also proposed to include an allowance for FNS to require an inventory transfer to another State distributing agency or processor when inventories are determined to be excessive for a State distributing agency or processor, i.e., more than six months on-hand or exceeding the established inventory protection, to ensure full utilization prior to the end of the school year.

Many comments were received on this provision. One commenter requested clarification that the inventory limit was not based on the average usage over a six-month period. That is correct. The inventory limit is intended to be based on average usage for the year being evaluated. Thus, the final rule is amended to clarify.

One commenter expressed concern that including a provision allowing FNS to transfer inventories to another State distributing agency or processor when inventories are determined to be excessive for a State distributing agency or processor will prevent a distributing agency from providing justification that accounts for the overage. This is not the intent of the proposed provision. Consistent with inventory transfers generally, inventory transfers due to excessive inventories will only occur after consultation with all the involved parties. The commenter also inquired whether advancements in technology and improvements in the Department's business practices will eventually eliminate the need for the six-month inventory limit. The Department consistently endeavors to improve our

service and the technology with which stakeholders interface. However, elimination of the current inventory limits is not currently proposed. Thus, the proposed language is retained without change in this final rule

One commenter requested that the six-month inventory limit be eliminated and that an annual three-month inventory carryover limit be imposed. Such a provision would require a separate rule and would be subject to public comment. Therefore, this language will not be included in the final rule.

Fourteen commenters requested that language be included in this provision to establish the method by which the six-month inventory level is calculated. Additionally, the commenters requested that average monthly usage, which is used to determine the six-month inventory limit, be calculated using a ten month period as opposed to a twelve month period. The commenters felt that a ten month period more accurately reflects the average school year and the period during which products are delivered. Although the six-month inventory limit is contained in current regulations, the method by which it is calculated is prescribed in a Policy Memorandum (FD-064; dated March 20, 2012). FNS will consider the position of the commenters and determine whether to issue program policy to reflect this change. Thus, the proposed language is retained without change in this final rule.

In § 250.35(e), we proposed to clarify that the distributing agency may permit the processor to carry over donated foods in excess of allowed levels into the next year of its agreement, if the distributing agency determines that the processor may efficiently process such foods.

We also proposed to include the distributing agency's current option to direct the processor to transfer or re-donate such donated foods to another distributing or recipient agency or processor. Lastly, we proposed to clarify that, if these options are not practical, the distributing agency must require the processor to pay for the donated foods held in excess of allowed levels in an amount equal to the replacement value of the donated foods. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.35(f), we proposed to expand the current options for the disposition of substitutable donated foods at the termination of an agreement to all donated foods, in accordance with our proposal in the proposed § 250.34 to permit substitution of all donated foods. We proposed to clarify that the disposition of donated foods may include a transfer; i.e., the distributing agency may permit a transfer of donated foods to another State distributing agency, with FNS approval, in accordance with current § 250.12(e). We also proposed to permit the transfer of commercially purchased foods that meet the substitution requirements in the proposed § 250.34 in place of the donated foods. We proposed to permit the processor to pay the distributing or recipient agency, as appropriate, for the donated foods only if returning or transferring the donated foods or commercially purchasing food that meets the substitution requirements is not feasible and if FNS approval has been granted. We proposed to include the current requirement that the processor pay the cost of transporting any donated foods when the agreement is terminated at the processor's request or as a result of the processor's failure to comply with the requirements of 7 CFR part 250. One commenter requested that the higher value not be used between the contract value and

replacement value when processors pay the distributing or recipient agency under § 250.35(f)(3). However, FNS wants to ensure that distributing and recipient agencies are made whole in these situations. Thus, the proposed language is retained without change in this final rule.

7. End product sales and crediting for the value of donated foods, § 250.36

In § 250.36, we proposed to describe the methods of end product sales. A processor must sell end products to recipient agencies under a system that assures such agencies receive credit or “value pass through” for the contract value of donated food contained in the end product. Processors must also ensure that, when end products are provided to commercial distributors for sale and delivery to recipient agencies, such sales occur under a system that provides such agencies with a credit for the contract value of donated food contained in the end product. In § 250.36(a), we proposed to require that the sales of end products, either directly by the processor or through a commercial distributor, be performed utilizing one of the methods of end product sales contained in this section, to ensure that the distributing or recipient agency, as appropriate, receives credit for the value of donated foods contained in end products. We also proposed to require that all systems of sales utilized must provide clear documentation of crediting for the value of the donated foods contained in the end products. One commenter requested that language be added to this provision that clarifies that method of end product sales is synonymous with value pass through system. Thus, the final rule is amended to clarify.

In § 250.36(b), we proposed to permit end product sales through a refund or rebate system, in which the processor or distributor sells end products to the distributing or recipient agency, as appropriate, at the commercial or gross price, and provides the appropriate agency with a refund for the contract value of donated foods contained in the end products. We proposed to require the processor to remit the refund to the distributing or recipient agency, as appropriate, within 30 days of receiving a request for a refund from the appropriate agency. We proposed to clarify that the refund request must be in writing but may be transmitted via e-mail or other electronic means. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.36(c), we proposed to permit end product sales through a discount system, in which the processor sells end products at a net price that provides a discount from the commercial case price for the value of the donated foods contained in the end products. We proposed to refer to this system as a direct discount system to distinguish it from the method of end product sales described in the following paragraph. One commenter requested that the word “provides” be replaced with “incorporates” to clarify the provision. Thus, the final rule is amended to clarify.

In § 250.36(d), we proposed to permit end product sales through a net price that provides a discount from the commercial case price for the value of the donated foods contained in the end products. The processor then compensates the distributor for the discount provided for the value of the donated food in its sale of end products. We proposed to refer to it as an indirect discount system. We proposed to require the processor to ensure that the distributor

notify it of such sales, at least on a monthly basis, through automated sales reports or other submissions. Fifteen commenters requested that the term “net off invoice” be incorporated into the provision to refer to the practice as it is commonly known. Thus, the final rule is amended to clarify. Twelve commenters requested that language be included in the provision to encourage recipient agencies to closely monitor invoices to ensure correct discounts are applied. Thus, the final rule is amended to clarify. One commenter requested that the word “provides” be replaced with “incorporates” to clarify the provision. Thus, the final rule is amended to clarify. One commenter requested that the frequency at which distributors must report end product sales to processors be increased from at least monthly to weekly. Not all distributors are currently capable of meeting that requirement. Moreover, such a provision would require a separate rule and would be subject to public comment. Therefore, this language will not be included in the final rule.

In § 250.36(e), we proposed to permit end product sales through a fee-for-service system, which includes all costs to produce the end product minus the value of the donated food put into production. The processor must identify any charge for delivery of end products separately from the fee-for-service on its invoice. One commenter requested clarification on how a processor would know a distributor’s delivery charge in order to identify it separately on its invoice. If the delivery charge is listed on the processor’s invoice, the processor may have procured the services of the distributor to store and/or deliver the product to the recipient. Therefore, the delivery charge would be known by the processor. If the processor did not procure the services of the distributor, the processor can request that the distributor directly bill the recipient agency for the distributor’s services. Thus, the proposed language

is retained without change in this final rule. Thirteen commenters requested that this provision be expanded to identify three distinct variations of fee-for-service. The commenters' preferred breakdown is: (1) Direct shipment and invoicing from the processor to the recipient agency; (2) Fee-for-service through a distributor, where the processor ships multiple pallets of product to a distributor with a breakout of who owns what products; and (3) What is commonly known as Modified Fee-for-service, when the recipient agency has an authorized agent bill them for the total case price. Thus, the final rule is amended to clarify.

In § 250.36(f), we proposed that the processor and distributor may sell end products to the distributing or recipient agency under an alternate method of end product sales that is approved by FNS and the distributing agency. Such alternate methods of sale must ensure that the distributing or recipient agency, as appropriate, receives credit for the value of donated foods contained in the end products. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.36(g), we proposed to clarify that the contract value of the donated foods must be used in crediting for donated foods in end product sales and to refer to the definition of contract value included in current § 250.2. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.36(h), we proposed to require that the distributing agency provide the processor with a list of recipient agencies eligible to purchase end products along with the quantity of

raw donated food that is to be delivered to the processor for processing on behalf of each recipient agency. This is intended to ensure that only eligible recipient agencies receive end products and that those end products are received only in the amounts for which they are eligible. For end products sold through distributors, we proposed to require that the processor provide the distributor with a list of eligible recipient agencies and either the quantities of approved end products that each recipient agency is eligible to receive or the quantity of donated food allocated to each recipient agency along with the raw donated food (pounds or cases) needed per case of each approved end product. One commenter expressed concern that this provision has the potential for abuse by processors because it may provide them with information that can be used for marketing and that it may impact deliveries for direct delivery donated foods. Processors and distributors must know which recipient agencies are eligible to receive end products containing donated foods to ensure that only eligible recipient agencies receive such products. FNS believes that processors will use this provision to promote the use of processed end products by recipient agencies but not to a degree that could be seen as abuse. Thus, the proposed language is retained without change in this final rule.

8. Reports, records, and reviews of processor performance, § 250.37

In § 250.37, we proposed to include the reporting and recordkeeping requirements for the processing of donated foods, and the use of such reports and records to review processor performance. In current § 250.30(m), the processor must submit a monthly performance report to the distributing agency, including the following information for the reporting period, with year-to-date totals:

- 1) A list of all eligible recipient agencies receiving end products;
- 2) The quantity of donated foods on hand at the beginning of the reporting period;
- 3) The quantity of donated foods received;
- 4) The quantity of donated foods transferred to the processor from another entity, or transferred by the processor to another entity;
- 5) The quantity of end products delivered to each eligible recipient agency; and
- 6) The quantity of donated foods remaining at the end of the reporting period.

In § 250.37(a), we proposed to retain the requirement that the processor submit the performance report to the distributing agency (or to the recipient agency, in accordance with a Recipient Agency Processing Agreement) on a monthly basis. We proposed to retain all of the currently required information in the report. We proposed to require the processor to also include quantities of donated food losses, and grading certificates and other documentation, as requested by the distributing agency, to support the information included in the performance reports. Such documentation may include, for example, bills of lading, invoices or copies of refund payments to verify sales and delivery of end products to recipient agencies. We proposed to retain the current deadlines for the submission of performance reports in the proposed § 250.37(a). Twelve commenters requested that the additional month for reporting year-end transactions be removed from the provision. The commenters felt that the advanced tracking methods instituted with improved technology permits processors to complete the necessary tasks without additional time and that this will assist state agencies in expediting the analysis of processor inventory. Thus, the final rule is amended accordingly. The commenters also requested clarification that a processor can stop

reporting on a given USDA Food to a state agency for products with a beginning balance of zero and by which there have been no receipts, adjustments, or shipments of end products for that USDA Foods code. This is a correct interpretation. FNS will explore policy guidance to provide clarification on this issue.

In § 250.37(b), we proposed to require that the processor must include reductions in donated food inventories on monthly performance reports only after sales of end products have been made or after sales of end products through distributors have been documented. We proposed to require that, when a distributor sells end products under a refund system, such documentation must be through the distributing or recipient agency's request for a refund (under a refund system) or through the distributor's automated sales reports or other electronic or written submission (under an indirect discount system or under fee-for-service). No comments were received on this provision. However, FNS received many comments on the proposed provision at § 250.11(e) and language was included in § 250.37(b) of this final rule to clarify the impact of that provision.

In § 250.37(c), we proposed to require that a multi-State processor submit a summary performance report to FNS, on a monthly basis and in a standard format established by FNS, containing information from the performance report that would allow FNS to track the processor's total and State-by-State donated food inventories. The purpose of this report is to assess the amount of the performance bond or letter of credit required of the processor under its National Processing Agreement. However, each distributing agency would still be responsible for monitoring the multi-State processor's inventory of donated foods received

for processing in the respective State, in accordance with the proposed § 250.37(a). No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.37(d), we proposed to require processors to maintain specific records to demonstrate compliance with processing requirements in 7 CFR part 250, including, for example, assurance of receipt of donated food shipments, production, sale, and delivery of end products, and crediting for donated foods contained in end products. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.37(e), we proposed to require distributing agencies to maintain specific records to demonstrate compliance with processing requirements in 7 CFR part 250, including, for example, end product data schedules, performance reports, copies of audits, and documentation of the correction of any deficiencies identified in such audits. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.37(f), we proposed to require that recipient agencies maintain specific records to demonstrate compliance with processing requirements in 7 CFR part 250, including, for example, the receipt of end products purchased from processors or distributors, crediting for the value of donated foods included in end products, and procurement documents. No

comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.37(g), we proposed to clarify the review requirements for the distributing agency including the review of performance reports to ensure that the processor:

- 1) Receives donated food shipments, as applicable;
- 2) Delivers end products to eligible recipient agencies, in the types and quantities for which they are eligible;
- 3) Meets the required processing yields for donated foods; and
- 4) Accurately reports donated food inventory activity and maintains inventories within approved levels.

No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

We proposed to remove the requirements in current § 250.30(m)(2) and (n)(2) relating to the submission of reports and the performance of reviews to ensure that substitution of concentrated skim milk for donated nonfat dry milk is in compliance with requirements.

Donated nonfat dry milk is no longer available for donation to schools. No comments were received on this removal. Thus, the proposed removal is retained without change in this final rule.

9. Provisions of agreements, § 250.38

In § 250.38, we proposed the required provisions for each type of processing agreement included in the proposed § 250.30, to ensure compliance with the requirements in 7 CFR part 250. In § 250.38(a), we proposed to establish that the National Processing Agreement is inclusive of all provisions necessary to ensure that a multi-State processor complies with all applicable requirements relating to the processing of donated foods. FNS has developed a prototype National Processing Agreement that includes all such required provisions. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.38(b), we proposed to require that the State Participation Agreement with a multi-State processor contain specific provisions or attachments to assure compliance with requirements in 7 CFR part 250 that are not included in the multi-State processor's National Processing Agreement. Such provisions include, for example, a list of recipient agencies eligible to receive end products, summary end product data schedules that contain a list of end products that may be sold in the State, a requirement that processors enter into a written agreement with distributors handling end products containing donated foods, and the allowed method(s) of end product sales implemented by the distributing agency. One commenter requested clarification that physical processor to processor transfers are not included in the term backhauled in § 250.38(b)(5). The commenter is correct that physical processor to processor transfers are not included in the term backhaul. The term backhauling is defined in the proposed § 250.2 to only include distributing or recipient agency origin. Thus, the proposed language is retained without change in this final rule.

In § 250.38(c), we proposed to require that the In-State Processing Agreement contain specific provisions or attachments to assure compliance with requirements in 7 CFR part 250, including assurance that the processor will meet processing yields for donated foods and substitution requirements, report donated food inventory activity and maintain inventories within approved levels, enter into a written agreement with distributors handling end products containing donated foods, credit recipient agencies for the value of all donated foods contained in end products, and obtain required audits. One commenter requested clarification on which party is responsible for holding the bond or irrevocable letter of credit for donated foods at the subcontractor of an in-State processor under the proposed § 250.38(c)(4). The distributing agency has discretion under an In-State Processing Agreement, including discretion in determining which party holds the bond or irrevocable letter of credit for donated foods at the subcontractor of an in-State processor. Thus, the proposed language is retained without change in this final rule.

In § 250.38(d), we proposed to require that the Recipient Agency Processing Agreement contain the same provisions as an In-State Processing Agreement, to the extent that the distributing agency permits the recipient to perform activities normally performed by the distributing agency under an In-State Processing Agreement (e.g., approval of end product data schedules or review of performance reports). However, a list of recipient agencies eligible to receive end products need not be included unless the Recipient Agency Processing Agreement represents more than one (e.g., a cooperative) recipient agency. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.38(e), we proposed to prohibit a distributing or recipient agency, as appropriate, from extending or renewing an agreement when a processor has not complied with processing requirements. We proposed to allow a distributing or recipient agency to immediately terminate an agreement in the event of such noncompliance. One commenter expressed concern that requiring an agency to terminate or not renew an agreement can cause hardship for either agency. The commenter felt that this should be at the discretion of the agency as extenuating circumstances may apply and processors may be able to rectify their issues and provide sufficient service the following year. Thus, the final rule is amended to allow distributing and recipient agencies discretion in determining whether or not to extend or renew agreements when a processor has not complied with processing requirements. However, these decisions will be evaluated by FNS during reviews of distributing and recipient agencies to ensure compliance with processing requirements.

10. Miscellaneous provisions, § 250.39

In § 250.39(a), we proposed that FNS may waive any of the requirements in 7 CFR part 250 for the purpose of conducting demonstration projects to test program changes which might improve processing of donated foods. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.39(b), we proposed to require the distributing agency to develop and provide a processing manual or similar materials to processors and other parties to ensure sufficient guidance is given regarding the requirements for the processing of donated foods.

Consistent with the current demonstration project, the distributing agency would be permitted to provide additional information relating to State-specific processing procedures upon request. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

In § 250.39(c), we proposed to clarify that guidance or information relating to the processing of donated foods is included on the FNS website or may otherwise be obtained from FNS. Such guidance and information includes program regulations and policies, the FNS Audit Guide, and the USDA National Processing Agreement. No comments were received on this provision. Thus, the proposed language is retained without change in this final rule.

### **III. Procedural Matters**

#### **A. Executive Orders 12866, 13563, and 13771**

Executive Orders 12866 and 13563 direct agencies to assess all costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits (including potential economic, environmental, public health and safety effects, distributive impacts, and equity). Executive Order 13563 emphasizes the importance of quantifying both costs and benefits, of reducing costs, of harmonizing rules, and of promoting flexibility. Executive Order 13771 directs agencies to reduce regulation and control regulatory costs and provides that for every one new regulation issued, at least two prior regulations be identified for elimination, and that the

cost of planned regulations be prudently managed and controlled through a budgeting process.

This final rule has been determined to be not significant and was not reviewed by the Office of Management and Budget (OMB) in conformance with Executive Order 12866.

FNS considers this rule to be an Executive Order 13771 deregulatory action.

#### B. Regulatory Impact Analysis

This rule has been designated as not significant by the Office of Management and Budget, therefore, no Regulatory Impact Analysis is required.

#### C. Regulatory Flexibility Act

The Regulatory Flexibility Act (5 U.S.C. 601-612) requires Agencies to analyze the impact of rulemaking on small entities and consider alternatives that would minimize any significant impacts on a substantial number of small entities. Pursuant to that review, the Administrator of FNS has certified that this rule would not have a significant impact on a substantial number of small entities.

#### D. Unfunded Mandates Reform Act

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 Department generally must prepare a written statement, including a cost benefit analysis, for proposed and final rules with “Federal mandates” that may result in expenditures by State, local or Tribal governments, in the aggregate, or 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 Department to identify and consider a reasonable number of regulatory alternatives and adopt the most cost effective or least burdensome alternative that achieves the objectives of the rule.

This final rule does not contain 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, the rule is not subject to the requirements of sections 202 and 205 of the UMRA.

#### E. Executive Order 12372

The donation of foods in USDA food distribution and child nutrition programs is included in the Catalog of Federal Domestic Assistance under 10.555, 10.558, 10.559, 10.565, 10.567, and 10.569 is subject to Executive Order 12372, which requires intergovernmental consultation with State and local officials. (See 2 CFR chapter IV)

#### F. Federalism Summary Impact Statement

Executive Order 13132 requires Federal agencies to consider the impact of their regulatory actions on State and local governments. Where such actions have federalism implications, agencies are directed to provide a statement for inclusion in the preamble to the regulations

describing the agency's considerations in terms of the three categories called for under Section (6)(b)(2)(B) of Executive Order 13121.

The Department has considered the impact of this rule on State and local governments and has determined that this rule does not have federalism implications. Therefore, under section 6(b) of the Executive Order, a federalism summary is not required.

#### G. Civil Rights Impact Analysis

FNS has reviewed this final rule in accordance with USDA Regulation 4300-4, "Civil Rights Impact Analysis," to identify any major civil rights impacts the rule might have on program participants on the basis of age, race, color, national origin, sex or disability. After a careful review of the rule's intent and provisions, FNS has determined that this rule would not in any way limit or reduce the ability of participants to receive the benefits of donated foods in food distribution or child nutrition programs on the basis of an individual's or group's race, color, national origin, sex, age, or disability. FNS found no factors that would negatively and disproportionately affect any group of individuals.

#### H. Executive Order 13175

Executive Order 13175 requires Federal agencies to consult and coordinate with Tribes on a government-to-government basis on policies that have Tribal implications, including regulations, legislative comments or proposed legislation, and other policy statements or actions that have substantial direct effects on one or more Indian Tribes, on the relationship between the Federal Government and Indian Tribes, or on the distribution of power and

responsibilities between the Federal Government and Indian Tribes. FNS consulted with Tribes on this proposed rule on November 19, 2014; however, no concerns or comments were received. We are unaware of any current Tribal laws that could conflict with the final rule.

#### I. Paperwork Reduction Act

The Paperwork Reduction Act of 1995 (44 U.S.C. Chap. 35) requires the Office of Management and Budget (OMB) to approve all collections of information by a Federal agency before they can be implemented. Respondents are not required to respond to any collection of information unless it displays a current, valid OMB control number. No changes have been made to the proposed information collection requirements in this final rulemaking. Thus, in accordance with the Paperwork Reduction Act of 1995, the information collection requirements associated with this final rule, which were filed under 0584-0293, have been submitted for approval to OMB. When OMB notifies FNS of its decision, FNS will publish a notice in the Federal Register of the action.

#### J. E-Government Act Compliance

The Department is committed to complying with the E-Government Act, to promote the use of the Internet and other information technologies to provide increased opportunities for citizen access to Government information and services, and for other purposes.

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

Administrative practice and procedure, Food assistance programs, Grant programs, Reporting and recordkeeping requirements, Social programs, 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 § 250.2:

a. Remove definitions of Contracting agency and Fee-for-service.

b. Add definitions in alphabetical order for Backhauling, Commingling, End product data schedule, In-State Processing Agreement, National Processing Agreement, Recipient Agency Processing Agreement, Replacement value, and State Participation Agreement.

The additions read as follows:

**§ 250.2 Definitions.**

\* \* \* \* \*

Backhauling means the delivery of donated foods to a processor for processing from a distributing or recipient agency's storage facility.

\* \* \* \* \*

Commingling means the storage of donated foods together with commercially purchased foods.

\* \* \* \* \*

End product data schedule means a processor's description of its processing of donated food into a finished end product, including the processing yield of donated food.

\* \* \* \* \*

In-State Processing Agreement means a distributing agency's agreement with an in-State processor to process donated foods into finished end products for sale to eligible recipient agencies or for sale to the distributing agency.

\* \* \* \* \*

National Processing Agreement means an agreement between FNS and a multi-State processor to process donated foods into end products for sale to distributing or recipient agencies.

\* \* \* \* \*

Recipient Agency Processing Agreement means a recipient agency's agreement with a processor to process donated foods and to purchase the finished end products.

\* \* \* \* \*

Replacement value means the price assigned by the Department to a donated food which must reflect the current price in the market to ensure compensation for donated foods lost in processing or other activities. The replacement value may be changed by the Department at any time.

\* \* \* \* \*

State Participation Agreement means a distributing agency's agreement with a multi-State processor to permit the sale of finished end products produced under the processor's National Processing Agreement to eligible recipient agencies in the State or to directly purchase such finished end products.

\* \* \* \* \*

3. In § 250.11, revise paragraph (e) to read as follows:

**§ 250.11 Delivery and receipt of donated food shipments.**

\* \* \* \* \*

(e) Transfer of title. In general, title to donated foods transfers to the distributing agency or recipient agency, as appropriate, upon acceptance of the donated foods at the time and place of delivery. Title to donated foods provided to a multi-State processor, in accordance with

its National Processing Agreement, transfers to the distributing agency or recipient agency, as appropriate, upon acceptance of the finished end products at the time and place of delivery. However, when a recipient agency has contracted with a distributor to act as an authorized agent, title to finished end products containing donated foods transfers to the recipient agency upon delivery and acceptance by the contracted distributor.

Notwithstanding transfer of title, distributing and recipient agencies must ensure compliance with the requirements of this part in the distribution, control, and use of donated foods.

4. In § 250.18, revise paragraph (b) to read as follows:

**§ 250.18 Reporting requirements.**

\* \* \* \* \*

(b) Processor performance. Processors must submit performance reports and other supporting documentation, as required by the distributing agency or by FNS, in accordance with § 250.37(a), to ensure compliance with requirements in this part.

\* \* \* \* \*

5. In § 250.19, revise paragraph (a) to read as follows:

**§ 250.19 Recordkeeping requirements.**

(a) Required records. Distributing agencies, recipient agencies, processors, and other entities must maintain records of agreements and contracts, reports, audits, and claim actions, funds obtained as an incident of donated food distribution, and other records specifically required in this part or in other Departmental regulations, as applicable. In

addition, distributing agencies must keep a record of the value of donated foods each of its school food authorities receives, in accordance with § 250.58(e), and records to demonstrate compliance with the professional standards for distributing agency directors established in § 235.11(g) of this chapter. Processors must also maintain records documenting the sale of end products to recipient agencies, including the sale of such end products by distributors, and must submit monthly performance reports, in accordance with subpart C of this part and with any other recordkeeping requirements included in their agreements. Specific recordkeeping requirements relating to the use of donated foods in contracts with food service management companies are included in § 250.54. Failure of the distributing agency, recipient agency, processor, or other entity to comply with recordkeeping requirements must be considered prima facie evidence of improper distribution or loss of donated foods and may result in a claim against such party for the loss or misuse of donated foods, in accordance with § 250.16, or in other sanctions or corrective actions.

\* \* \* \* \*

6. Revise Subpart C to read as follows:

**Subpart C—Processing of Donated Foods**

250.30 Processing of donated foods into end products.

250.31 Procurement requirements.

250.32 Protection of donated food value.

250.33 Ensuring processing yields of donated foods.

250.34 Substitution of donated foods.

250.35 Storage, food safety, quality control, and inventory management.

250.36 End product sales and crediting for the value of donated foods.

250.37 Reports, records, and reviews of processor performance.

250.38 Provisions of agreements.

250.39 Miscellaneous provisions.

### **Subpart C—Processing of Donated Foods**

#### **§ 250.30 Processing of donated foods into end products.**

(a) Purpose of processing donated foods. Donated foods are most commonly provided to processors to process into approved end products for use in school lunch programs or other food services provided by recipient agencies. The ability to divert donated foods for processing provides recipient agencies with more options for using donated foods in their programs. For example, donated foods such as whole chickens or chicken parts may be processed into precooked grilled chicken strips for use in the National School Lunch Program. In some cases, donated foods are provided to processors to prepare meals or for repackaging. Use of a commercial facility to repackage donated foods, or to use donated foods in the preparation of meals, is considered processing in this part.

(b) Agreement requirement. The processing of donated foods must be performed in accordance with an agreement between the processor and FNS, between the processor and the distributing agency, or, if allowed by the distributing agency, between the processor and a recipient agency or subdistributing agency. However, a processing agreement will not obligate any party to provide donated foods to a processor for processing. The agreements described below are required in addition to, not in lieu of, competitively procured contracts

required in accordance with § 250.31. The processing agreement must be signed by an authorized individual for the processor. The different types of processing agreements are described in this section.

(c) National Processing Agreement. A multi-State processor must enter into a National Processing Agreement with FNS in order to process donated foods into end products in accordance with end product data schedules approved by FNS. FNS also holds and manages such processor's performance bond or letter of credit under its National Processing Agreement, in accordance with § 250.32. FNS does not itself procure or purchase end products under a National Processing Agreement. A multi-State processor must also enter into a State Participation Agreement with the distributing agency in order to sell nationally approved end products in the State, in accordance with paragraph (d) of this section.

(d) State Participation Agreement. The distributing agency must enter into a State Participation Agreement with a multi-State processor to permit the sale of end products produced under the processor's National Processing Agreement to eligible recipient agencies in the State or to directly purchase such end products. The distributing agency may include other State-specific processing requirements in its State Participation Agreement, such as the methods of end product sales permitted, in accordance with § 250.36, or the use of labels attesting to fulfillment of meal pattern requirements in child nutrition programs. The distributing agency must utilize the following criteria in its selection of processors with which it enters into agreements. These criteria will be reviewed by the appropriate FNS Regional Office during the management evaluation review of the distributing agency.

- (1) The nutritional contribution provided by end products;
- (2) The marketability or acceptability of end products;
- (3) The means by which end products will be distributed;
- (4) Price competitiveness of end products and processing yields of donated foods;
- (5) Any applicable labeling requirements; and
- (6) The processor's record of ethics and integrity, and capacity to meet regulatory requirements.

(e) In-State Processing Agreement. A distributing agency must enter into an In-State Processing Agreement with an in-State processor to process donated foods into finished end products, unless it permits recipient agencies to enter into Recipient Agency Processing Agreements for such purpose, in accordance with paragraph (f) of this section. Under an In-State Processing Agreement, the distributing agency approves end product data schedules (except red meat and poultry) submitted by the processor, holds and manages the processor's performance bond or letter of credit, in accordance with § 250.32, and assures compliance with other processing requirements. The distributing agency may also purchase the finished end products for distribution to eligible recipient agencies in the State under an In-State Processing Agreement, or may permit recipient agencies to purchase such end products, in accordance with applicable procurement requirements. In the latter case, the In-State Processing Agreement is often called a "master agreement." A distributing agency that procures end products on behalf of recipient agencies, or that limits recipient agencies' access to the procurement of specific end products through its master agreements, must utilize the following criteria in its selection of processors with which it enters into

agreements. These criteria will be reviewed by the appropriate FNS Regional Office during the management evaluation review of the distributing agency.

- (1) The nutritional contribution provided by end products;
- (2) The marketability or acceptability of end products;
- (3) The means by which end products will be distributed;
- (4) Price competitiveness of end products and processing yields of donated foods;
- (5) Any applicable labeling requirements; and
- (6) The processor's record of ethics and integrity, and capacity to meet regulatory requirements.

(f) Recipient Agency Processing Agreement. The distributing agency may permit a recipient agency to enter into an agreement with an in-State processor to process donated foods and to purchase the finished end products in accordance with a Recipient Agency Processing Agreement. A recipient agency may also enter into a Recipient Agency Processing Agreement on behalf of other recipient agencies, in accordance with an agreement between the parties. The distributing agency may also delegate a recipient agency to approve end product data schedules or select nationally approved end product data schedules, review in-State processor performance reports, manage the performance bond or letter of credit of an in-State processor, and monitor other processing activities under a Recipient Agency Processing Agreement. All such activities must be performed in accordance with the requirements of this part. All Recipient Agency Processing Agreements must be reviewed and approved by the distributing agency. All recipient

agencies must utilize the following criteria in its selection of processors with which it enters into agreements:

- (1) The nutritional contribution provided by end products;
- (2) The marketability or acceptability of end products;
- (3) The means by which end products will be distributed;
- (4) Price competitiveness of end products and processing yields of donated foods;
- (5) Any applicable labeling requirements; and
- (6) The processor's record of ethics and integrity, and capacity to meet regulatory requirements.

(g) Ensuring acceptability of end products. A distributing agency that procures end products on behalf of recipient agencies, or that otherwise limits recipient agencies' access to the procurement of specific end products, must provide for testing of end products to ensure their acceptability by recipient agencies, prior to entering into processing agreements. End products that have previously been tested, or that are otherwise determined to be acceptable, need not be tested. However, such a distributing agency must monitor product acceptability on an ongoing basis.

(h) Prohibition against subcontracting. A processor may not assign any processing activities under its processing agreement or subcontract to another entity to perform any aspect of processing, without the specific written consent of the other party to the agreement (i.e., distributing or recipient agency, or FNS, as appropriate). The distributing agency may, for

example, provide the required consent as part of its State Participation Agreement or In-State Processing Agreement with the processor.

(i) Agreements between processors and distributors. A processor providing end products containing donated foods to a distributor must enter into a written agreement with the distributor. The agreement must reference, at a minimum, the financial liability (i.e., who must pay) for the replacement value of donated foods, not less than monthly end product sales reporting frequency, requirements under § 250.11, and the applicable value pass through system to ensure that the value of donated foods and finished end products are properly credited to recipient agencies. Distributing agencies can set additional requirements.

(j) Duration of agreements. In-State Processing Agreements and Recipient Agency Processing Agreements may be up to five years in duration. State Participation Agreements may be permanent. National Processing Agreements are permanent. Amendments to any agreements may be made, as needed, with the concurrence of both parties to the agreement. Such amendments will be effective for the duration of the agreement, unless otherwise indicated.

### **§ 250.31 Procurement requirements.**

(a) Applicability of Federal procurement requirements. Distributing and recipient agencies must comply with the requirements in 2 CFR part 200 and part 400, as applicable, in purchasing end products, distribution, or other processing services from processors.

Distributing and recipient agencies may use procurement procedures that conform to applicable State or local laws and regulations, but must ensure compliance with the procurement requirements in 2 CFR part 200 and part 400, as applicable.

(b) Required information in procurement documents. In all procurements of processed end products containing USDA donated foods, procurement documents must include the following information:

- (1) The price to be charged for the end product or other processing service;
- (2) The method of end product sales that will be utilized and assurance that crediting for donated foods will be performed in accordance with the applicable requirements for such method of sales in § 250.36;
- (3) The value of the donated food in the end products; and
- (4) The location for the delivery of the end products.

**§ 250.32 Protection of donated food value.**

(a) Performance bond or irrevocable letter of credit. The processor must obtain a performance bond or an irrevocable letter of credit to protect the value of donated foods to be received for processing prior to the delivery of the donated foods to the processor. The processor must provide the performance bond or letter of credit to the distributing or recipient agency, in accordance with its In-State or Recipient Agency Processing Agreement. However, a multi-State processor must provide the performance bond or letter of credit to FNS, in accordance with its National Processing Agreement. For multi-State processors, the minimum amount of the performance bond or letter of credit must be

sufficient to cover at least 75 percent of the value of donated foods in the processor's physical or book inventory, as determined annually and at the discretion of FNS for processors under National Processing Agreements. For multi-state processors in their first year of participation in the processing program, the amount of the performance bond or letter of credit must be sufficient to cover 100 percent of the value of donated foods, as determined annually, and at the discretion of FNS. The surety company from which a bond is obtained must be listed in the most current Department of Treasury's Listing of Approved Sureties (Department Circular 570).

(b) Calling in the performance bond or letter of credit. The distributing or recipient agency must call in the performance bond or letter of credit whenever a processor's lack of compliance with this part, or with the terms of the In-State or Recipient Agency Processing Agreement, results in a loss of donated foods to a distributing or recipient agency and the processor fails to make restitution or respond to a claim action initiated to recover the loss. Similarly, FNS will call in the performance bond or letter of credit in the same circumstances, in accordance with National Processing Agreements, and will ensure that any monies recovered are reimbursed to distributing agencies for losses of entitlement foods.

**§ 250.33 Ensuring processing yields of donated foods.**

(a) End product data schedules. The processor must submit an end product data schedule, in a standard electronic format dictated by FNS, for approval before it may process donated foods into end products. For In-State Processing Agreements, the end product data schedule

must be approved by the distributing agency and, for products containing donated red meat and poultry, the end product data schedule must also be approved by the Department. For National Processing Agreements, the end product data schedule must be approved by the Department. An end product data schedule must be submitted, and approved, for each new end product that a processor wishes to provide or for a previously approved end product in which the ingredients (or other pertinent information) have been altered. On the end product data schedule, the processor must describe its processing of donated food into an end product, including the following information:

- (1) A description of the end product;
- (2) The types and quantities of donated foods included;
- (3) The types and quantities of other ingredients included;
- (4) The quantity of end product produced; and
- (5) The processing yield of donated food, which may be expressed as the quantity (pounds or cases) of donated food needed to produce a specific quantity of end product or as the percentage of raw donated food versus the quantity returned in the finished end product.

(b) Processing yields of donated foods. All end products must have a processing yield of donated foods associated with its production and this processing yield must be indicated on its end product data schedule. The processing yield options are limited to 100 percent yield, guaranteed yield, and standard yield.

- (1) Under 100 percent yield, the processor must ensure that 100 percent of the raw donated food is returned in the finished end product. The processor must replace any processing loss of donated food with commercially purchased food of the same generic identity, of U.S.

origin, and equal or better in all USDA procurement specifications than the donated food.

The processor must demonstrate such replacement by reporting reductions in donated food inventories on performance reports by the amount of donated food contained in the finished end product rather than the amount that went into production. The Department may approve an exception if a processor experiences a significant manufacturing loss.

(2) Under guaranteed yield, the processor must ensure that a specific quantity of end product (i.e., number of cases) will be produced from a specific quantity of donated food (i.e., pounds), as determined by the parties to the processing agreement, and, for In-State Processing Agreements, approved by the Department. If necessary, the processor must use commercially purchased food of the same generic identity, of U.S. origin, and equal or better in all USDA procurement specifications than the donated food to provide the guaranteed number of cases of end product to the distributing or recipient agency, as appropriate. The guaranteed yield must be indicated on the end product data schedule.

(3) Under standard yield, the processor must ensure that a specific quantity of end product (i.e., number of cases), as determined by the Department, will be produced from a specific quantity of donated food. The established standard yield is higher than the yield the processor could achieve under normal commercial production and serves to reward those processors that can process donated foods most efficiently. If necessary, the processor must use commercially purchased food of the same generic identity, of U.S. origin, and equal or better in all USDA procurement specifications than the donated food to provide the number of cases required to meet the standard yield to the distributing or recipient agency, as appropriate. The standard yield must be indicated on the end product data schedule.

(c) Compensation for loss of donated foods. The processor must compensate the distributing or recipient agency, as appropriate, for the loss of donated foods, or for the loss of commercially purchased foods substituted for donated foods. Such loss may occur, for example, if the processor fails to meet the required processing yield of donated food or fails to produce end products that meet required specifications, if donated foods are spoiled, damaged, or otherwise adulterated at a processing facility, or if end products are improperly distributed. To compensate for such loss, the processor must:

(1) Replace the lost donated food or commercial substitute with commercially purchased food of the same generic identity, of U.S. origin, and equal or better in all USDA procurement specifications than the donated food; or

(2) Return end products that are wholesome but do not meet required specifications to production for processing into the requisite quantity of end products that meet the required specifications (commonly called rework products); or

(3) If the purchase of replacement foods or the reprocessing of products that do not meet the required specifications is not feasible, the processor may, with FNS, distributing agency, or recipient agency approval, dependent on which entity maintains the agreement with the processor, pay the distributing or recipient agency, as appropriate, for the replacement value of the donated food or commercial substitute.

(d) Credit for sale of by-products. The processor must credit the distributing or recipient agency, as appropriate, for the sale of any by-products produced in the processing of donated foods. The processor must credit for the net value of such sale, or the market value of the by-products, after subtraction of any documented expenses incurred in preparing the

by-product for sale. Crediting must be achieved through invoice reduction or by another means of crediting.

(e) Labeling requirements. The processor must ensure that all end product labels meet Federal labeling requirements. A processor that claims end products fulfill meal pattern requirements in child nutrition programs must comply with the procedures required for approval of labels of such end products.

#### **§ 250.34 Substitution of donated foods.**

(a) Substitution of commercially purchased foods for donated foods. Unless its agreement specifically stipulates that the donated foods must be used in processing, the processor may substitute commercially purchased foods for donated foods that are delivered to it from a USDA vendor. The commercially purchased food must be of the same generic identity, of U.S. origin, and equal or better in all USDA procurement specifications than the donated food. Commercially purchased beef, pork, or poultry must meet the same specifications as donated product, including inspection, grading, testing, and humane handling standards and must be approved by the Department in advance of substitution. The processor may choose to make the substitution before the actual receipt of the donated food. However, the processor assumes all risk and liability if, due to changing market conditions or other reasons, the Department's purchase of donated foods and their delivery to the processor is not feasible. Commercially purchased food substituted for donated food must meet the same processing yield requirements in § 250.33 that would be required for the donated food.

(b) Prohibition against substitution and other requirements for backhauled donated foods.

The processor may not substitute or commingle donated foods that are backhauled to it from a distributing or recipient agency's storage facility. The processor must process backhauled donated foods into end products for sale and delivery to the distributing or recipient agency that provided them and not to any other agency. Distributing or recipient agencies must purchase end products utilizing donated foods backhauled to their contracted processor.

The processor may not provide payment for backhauled donated foods in lieu of processing.

(c) Grading requirements. The processing of donated beef, pork, and poultry must occur under Federal Quality Assessment Division grading, which is conducted by the Department's Agricultural Marketing Service. Federal Quality Assessment Division grading ensures that processing is conducted in compliance with substitution and yield requirements and in conformance with the end product data schedule. The processor is responsible for paying the cost of acceptance service grading. The processor must maintain grading certificates and other records necessary to document compliance with requirements for substitution of donated foods and with other requirements of this subpart.

(d) Waiver of grading requirements. The distributing agency may waive the grading requirement for donated beef, pork or poultry in accordance with one of the conditions listed in this paragraph (d). However, grading may only be waived on a case by case basis (e.g., for a particular production run); the distributing agency may not approve a blanket waiver of the requirement. Additionally, a waiver may only be granted if a processor's past

performance indicates that the quality of the end product will not be adversely affected. The conditions for granting a waiver include:

- (1) That even with ample notification time, the processor cannot secure the services of a grader;
- (2) The cost of the grader's service in relation to the value of donated beef, pork or poultry being processed would be excessive; or
- (3) The distributing or recipient agency's urgent need for the product leaves insufficient time to secure the services of a grader.

(e) Use of substituted donated foods. The processor may use donated foods that have been substituted with commercially purchased foods in other processing activities conducted at its facilities.

**§ 250.35 Storage, food safety, quality control, and inventory management.**

(a) Storage and quality control. The processor must ensure the safe and effective storage of donated foods, including compliance with the general storage requirements in § 250.12, and must maintain an effective quality control system at its processing facilities.

The processor must maintain documentation to verify the effectiveness of its quality control system and must provide such documentation upon request.

(b) Food safety requirements. The processor must ensure that all processing of donated foods is conducted in compliance with all Federal, State, and local requirements relative to food safety.

(c) Commingling of donated foods and commercially purchased foods. The processor may commingle donated foods and commercially purchased foods, unless the processing agreement specifically stipulates that the donated foods must be used in processing, and not substituted, or the donated foods have been backhauled from a recipient agency. However, such commingling must be performed in a manner that ensures the safe and efficient use of donated foods, as well as compliance with substitution requirements in § 250.34 and with reporting of donated food inventories on performance reports, as required in § 250.37. The processor must also ensure that commingling of processed end products and other food products, either at its facility or at the facility of a commercial distributor, ensures the sale and delivery of end products that meet the processing requirements in this subpart—e.g., by affixing the applicable USDA certification stamp to the exterior shipping containers of such end products.

(d) Limitation on donated food inventories. Inventories of donated food at processors may not be in excess of a six-month supply, based on an average amount of donated foods utilized, unless a higher level has been specifically approved by the distributing agency on the basis of a written justification submitted by the processor. Distributing agencies are not permitted to submit food orders for processors reporting no sales activity during the prior year's contract period unless documentation is submitted by the processor which outlines specific plans for donated food drawdown, product promotion, or sales expansion. When inventories are determined to be excessive for a State or processor, e.g., more than six months or exceeding the established protection, FNS may require the transfer of inventory

and/or entitlement to another State or processor to ensure utilization prior to the end of the school year.

(e) Reconciliation of excess donated food inventories. If, at the end of the school year, the processor has donated food inventories in excess of a six-month supply, the distributing agency may, in accordance with paragraph (d) of this section, permit the processor to carry over such excess inventory into the next year of its agreement, if it determines that the processor may efficiently store and process such quantity of donated foods. The distributing agency may also direct the processor to transfer such donated foods to other recipient agencies, or to transfer them to other distributing agencies, in accordance with § 250.12(e). However, if these actions are not practical, the distributing agency must require the processor to pay it for the donated foods held in excess of allowed levels at the replacement value of the donated foods.

(f) Disposition of donated food inventories upon agreement termination. When an agreement terminates, and is not extended or renewed, the processor must take one of the actions indicated in this paragraph (f) with respect to remaining donated food inventories, as directed by the distributing agency or recipient agency, as appropriate. The processor must pay the cost of transporting any donated foods when the agreement is terminated at the processor's request or as a result of the processor's failure to comply with the requirements of this part. The processor must:

(1) Return the donated foods, or commercially purchased foods that meet the substitution requirements in § 250.34, to the distributing or recipient agency, as appropriate; or

(2) Transfer the donated foods, or commercially purchased foods that meet the substitution requirements in § 250.34, to another distributing or recipient agency with which it has a processing agreement; or

(3) If returning or transferring the donated foods, or commercially purchased foods that meet the substitution requirements in § 250.34, is not feasible, the processor may, with FNS approval, pay the distributing or recipient agency, as appropriate, for the donated foods, at the contract value or replacement value of the donated foods, whichever is higher.

**§ 250.36 End product sales and crediting for the value of donated foods.**

(a) Methods of end product sales. To ensure that the distributing or recipient agency, as appropriate, receives credit for the value of donated foods contained in end products, the sale of end products must be performed using one of the methods of end product sales, also known as value pass through systems, described in this section. All systems of sales utilized must provide clear documentation of crediting for the value of the donated foods contained in the end products.

(b) Refund or rebate. Under this system, the processor sells end products to the distributing or recipient agency, as appropriate, at the commercial, or gross, price and must provide a refund or rebate for the value of the donated food contained in the end products. The processor may also deliver end products to a commercial distributor for sale to distributing or recipient agencies under this system. In both cases, the processor must provide a refund to the appropriate agency within 30 days of receiving a request for a refund from that agency. The refund request must be in writing, which may be transmitted via e-mail or other electronic submission.

(c) Direct discount. Under this system, the processor must sell end products to the distributing or recipient agency, as appropriate, at a net price that incorporates a discount from the commercial case price for the value of donated food contained in the end products.

(d) Indirect discount. Under this system, also known as net off invoice, the processor delivers end products to a commercial distributor, which must sell the end products to an eligible distributing or recipient agency, as appropriate, at a net price that incorporates a discount from the commercial case price for the value of donated food contained in the end products. The processor must require the distributor to notify it of such sales, at least on a monthly basis, through automated sales reports or other electronic or written submission. The processor then compensates the distributor for the discount provided for the value of the donated food in its sale of end products. Recipient agencies should closely monitor invoices to ensure correct discounts are applied.

(e) Fee-for-service. (1) Under this system, the processor must sell end products to the distributing or recipient agency, as appropriate, at a fee-for-service, which includes all costs to produce the end products not including the value of the donated food used in production.

Three basic types of fee-for-service are used:

(i) Direct shipment and invoicing from the processor to the recipient agency;

(ii) Fee-for-service through a distributor, where the processor ships multiple pallets of product to a distributor with a breakout of who owns what products; and

(iii) What is commonly known as Modified Fee-for-service, when the recipient agency has an authorized agent bill them for the total case price.

(2) The processor must identify any charge for delivery of end products separately from the fee-for-service on its invoice. If the processor provides end products sold under fee-for-service to a distributor for delivery to the distributing or recipient agency, the processor must identify the distributor's delivery charge separately from the fee-for-service on its invoice to the appropriate agency or may permit the distributor to bill the agency separately for the delivery of end products. The processor must require that the distributor notify it of such sales, at least on a monthly basis, through automated sales reports, e-mail, or other electronic or written submission. When the recipient agency procures storage and distribution of processed end products separately from the processing of donated foods, the recipient agency may provide the distributor written approval to act as the recipient agency's authorized agent for the total case price (i.e., including the fee-for-service and the delivery charge), in accordance with § 250.11(e).

(f) Approved alternative method. The processor or distributor may sell end products under an alternative method approved by FNS and the distributing agency that ensures crediting for the value of donated foods contained in the end products.

(g) Donated food value used in crediting. In crediting for the value of donated foods in end product sales, the contract value of the donated foods, as defined in § 250.2, must be used.

(h) Ensuring sale and delivery of end products to eligible recipient agencies. In order to ensure the sale of end products to eligible recipient agencies, the distributing agency must provide the processor with a list of recipient agencies eligible to purchase end products,

along with the quantity of raw donated food that is to be delivered to the processor for processing on behalf of each recipient agency. In order to ensure that the distributor sells end products only to eligible recipient agencies, the processor must provide the distributor with a list of eligible recipient agencies and either:

(1) The quantities of approved end products that each recipient agency is eligible to receive;

or

(2) The quantity of donated food allocated to each recipient agency and the raw donated food (pounds or cases) needed per case of each approved end product.

**§ 250.37 Reports, records, and reviews of processor performance.**

(a) Performance reports. The processor must submit a performance report to the distributing agency (or to the recipient agency, in accordance with a Recipient Agency Processing Agreement) on a monthly basis, which must include the information listed in this paragraph

(a). Performance reports must be submitted not later than 30 days after the end of the reporting period. The performance report must include the following information for the reporting period, with year-to-date totals:

(1) A list of all recipient agencies purchasing end products;

(2) The quantity of donated foods in inventory at the beginning of the reporting period;

(3) The quantity of donated foods received;

(4) The quantity of donated foods transferred to the processor from another entity, or transferred by the processor to another entity;

(5) The quantity of donated foods losses;

(6) The quantity of end products delivered to each eligible recipient agency;

- (7) The quantity of donated foods remaining at the end of the reporting period;
- (8) A certification statement that sufficient donated foods are in inventory or on order to account for the quantities needed for production of end products;
- (9) Grading certificates, as applicable; and
- (10) Other supporting documentation, as required by the distributing agency or recipient agency.

(b) Reporting reductions in donated food inventories. The processor must report reductions in donated food inventories on performance reports only after sales of end products have been made, or after sales of end products through distributors have been documented.

However, when a recipient agency has contracted with a distributor to act as an authorized agent, the processor may report reductions in donated food inventories upon delivery and acceptance by the contracted distributor, in accordance with § 250.11(e). Documentation of distributor sales must be through the distributing or recipient agency's request for a refund (under a refund or rebate system) or through receipt of the distributor's automated sales reports or other electronic or written reports submitted to the processor (under an indirect discount system or under a fee-for-service system).

(c) Summary performance report. Along with the submission of performance reports to the distributing agency, a multi-State processor must submit a summary performance report to FNS, on a monthly basis and in a format established by FNS, in accordance with its National Processing Agreement. The summary report must include an accounting of the processor's national inventory of donated foods, including the information listed in this

paragraph (c). The report must be submitted not later than 30 days after the end of the reporting period; however, the final performance report must be submitted within 60 days of the end of the reporting period. The summary performance report must include the following information for the reporting period:

- (1) The total donated food inventory by State and the national total at the beginning of the reporting period;
- (2) The total quantity of donated food received by State, with year-to-date totals, and the national total of donated food received;
- (3) The total quantity of donated food reduced from inventory by State, with year-to-date totals, and the national total of donated foods reduced from inventory; and
- (4) The total quantity of donated foods remaining in inventory by State, and the national total, at the end of the reporting period.

(d) Recordkeeping requirements for processors. The processor must maintain the following records relating to the processing of donated foods:

- (1) End product data schedules and summary end product data schedules, as applicable;
- (2) Receipt of donated foods shipments;
- (3) Production, sale, and delivery of end products, including sales through distributors;
- (4) All agreements with distributors;
- (5) Remittance of refunds, invoices, or other records that assure crediting for donated foods in end products and for sale of byproducts;
- (6) Documentation of Federal or State inspection of processing facilities, as appropriate, and of the maintenance of an effective quality control system;

(7) Documentation of substitution of commercial foods for donated foods, including grading certificates, as applicable;

(8) Waivers of grading requirements, as applicable; and

(9) Required reports.

(e) Recordkeeping requirements for the distributing agency. The distributing agency must maintain the following records relating to the processing of donated foods:

(1) In-State Processing Agreements and State Participation Agreements;

(2) End product data schedules or summary end product data schedules, as applicable;

(3) Performance reports;

(4) Grading certificates, as applicable;

(5) Documentation that supports information on the performance report, as required by the distributing agency (e.g., sales invoices or copies of refund payments);

(6) Copies of audits of in-State processors and documentation of the correction of any deficiencies identified in such audits;

(7) The receipt of end products, as applicable; and

(8) Procurement documents, as applicable.

(f) Recordkeeping requirements for the recipient agency. The recipient agency must maintain the following records relating to the processing of donated foods:

(1) The receipt of end products purchased from processors or distributors;

(2) Crediting for the value of donated foods contained in end products;

(3) Recipient Agency Processing Agreements, as applicable, and, in accordance with such agreements, other records included in paragraph (e) of this section, if not retained by the distributing agency; and

(4) Procurement documents, as applicable.

(g) Review requirements for the distributing agency. The distributing agency must review performance reports and other records that it must maintain, in accordance with the requirements in paragraph (e) of this section, to ensure that the processor:

(1) Receives donated food shipments;

(2) Delivers end products to eligible recipient agencies, in the types and quantities for which they are eligible;

(3) Meets the required processing yields for donated foods; and

(4) Accurately reports donated food inventory activity and maintains inventories within approved levels.

### **§ 250.38 Provisions of agreements.**

(a) National Processing Agreement. A National Processing Agreement includes provisions to ensure that a multi-State processor complies with all of the applicable requirements in this part relating to the processing of donated foods.

(b) Required provisions for State Participation Agreement. A State Participation Agreement with a multi-State processor must include the following provisions:

- (1) Contact information for all appropriate parties to the agreement;
- (2) The effective dates of the agreement;
- (3) A list of recipient agencies eligible to receive end products;
- (4) Summary end product data schedules, with end products that may be sold in the State;
- (5) Assurance that the processor will not substitute or commingle backhauled donated foods and will provide end products processed from such donated foods only to the distributing or recipient agency from which the foods were received;
- (6) Any applicable labeling requirements;
- (7) Other processing requirements implemented by the distributing agency, such as the specific method(s) of end product sales permitted;
- (8) A statement that the agreement may be terminated by either party upon 30 days' written notice;
- (9) A statement that the agreement may be terminated immediately if the processor has not complied with its terms and conditions; and
- (10) A statement requiring the processor to enter into an agreement with any and all distributors delivering processed end products to recipient agencies that ensures adequate data sharing, reporting, and crediting of donated foods, in accordance with § 250.30(i).

(c) Required provisions of the In-State Processing Agreement. An In-State Processing Agreement must include the following provisions or attachments:

- (1) Contact information for all appropriate parties to the agreement;
- (2) The effective dates of the agreement;
- (3) A list of recipient agencies eligible to receive end products, as applicable;

- (4) In the event that subcontracting is allowed, the specific activities that will be performed under subcontracts;
- (5) Assurance that the processor will provide a performance bond or irrevocable letter of credit to protect the value of donated foods it is expected to maintain in inventory, in accordance with § 250.32;
- (6) End product data schedules for all end products, with all required information, in accordance with § 250.33(a);
- (7) Assurance that the processor will meet processing yields for donated foods, in accordance with § 250.33;
- (8) Assurance that the processor will compensate the distributing or recipient agency, as appropriate, for any loss of donated foods, in accordance with § 250.33(c);
- (9) Any applicable labeling requirements;
- (10) Assurance that the processor will meet requirements for the substitution of commercially purchased foods for donated foods, including grading requirements, in accordance with § 250.34;
- (11) Assurance that the processor will not substitute or commingle backhauled donated foods and will provide end products processed from such donated foods only to the recipient agency from which the foods were received, as applicable;

- (12) Assurance that the processor will provide for the safe and effective storage of donated foods, meet inspection requirements, and maintain an effective quality control system at its processing facilities;
- (13) Assurance that the processor will report donated food inventory activity and maintain inventories within approved levels;
- (14) Assurance that the processor will return, transfer, or pay for, donated food inventories remaining upon termination of the agreement, in accordance with § 250.35(f);
- (15) The specific method(s) of end product sales permitted, in accordance with § 250.36;
- (16) Assurance that the processor will credit recipient agencies for the value of all donated foods, in accordance with § 250.36;
- (17) Assurance that the processor will submit performance reports and meet other reporting and recordkeeping requirements, in accordance with § 250.37;
- (18) Assurance that the processor will obtain independent CPA audits and will correct any deficiencies identified in such audits, in accordance with § 250.20;
- (19) A statement that the distributing agency, subdistributing agency, or recipient agency, the Comptroller General, the Department of Agriculture, or their duly authorized representatives, may perform on-site reviews of the processor's operation to ensure that all activities relating to donated foods are performed in accordance with the requirements in 7 CFR part 250;
- (20) A statement that the agreement may be terminated by either party upon 30 days' written notice;
- (21) A statement that the agreement may be terminated immediately if the processor has not complied with its terms and conditions;

(22) A statement that extensions or renewals of the agreement, if applicable, are contingent upon the fulfillment of all agreement provisions; and

(23) A statement requiring the processor to enter into an agreement with any and all distributors delivering processed end products to recipient agencies that ensures adequate data sharing, reporting, and crediting of donated foods, in accordance with § 250.30(i).

(d) Required provisions for Recipient Agency Processing Agreement. The Recipient Agency Processing Agreement must contain the same provisions as an In-State Processing Agreement, to the extent that the distributing agency permits the recipient agency to perform activities normally performed by the distributing agency under an In-State Processing Agreement (e.g., approval of end product data schedules, review of performance reports, or management of the performance bond). However, a list of recipient agencies eligible to receive end products need not be included unless the Recipient Agency Processing Agreement represents more than one (e.g., a cooperative) recipient agency.

(e) Noncompliance with processing requirements. If the processor has not complied with processing requirements, the distributing or recipient agency, as appropriate, may choose to not extend or renew the agreement and may immediately terminate it.

**§ 250.39 Miscellaneous provisions.**

(a) Waiver of processing requirements. The Food and Nutrition Service may waive any of the requirements contained in this part for the purpose of conducting demonstration projects to test program changes designed to improve the processing of donated foods.

(b) Processing activity guidance. Distributing agencies must develop and provide a processing manual or similar procedural material for guidance to contracting agencies, recipient agencies, and processors. Distributing agencies must revise these materials as necessary to reflect policy and regulatory changes. This guidance material must be provided to contracting agencies, recipient agencies, and processors at the time of the approval of the initial agreement by the distributing agency, when there have been regulatory or policy changes which necessitate changes in the guidance materials, and upon request. The manual must include, at a minimum, statements of the distributing agency's policies and procedures regarding:

- (1) Contract approval;
- (2) Monitoring and review of processing activities;
- (3) Recordkeeping and reporting requirements;
- (4) Inventory controls; and
- (5) Refund applications.

(c) Guidance or information. Guidance or information relating to the processing of donated foods is included on the FNS website or may otherwise be obtained from FNS.

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