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## DEPARTMENT OF AGRICULTURE

### Agricultural Marketing Service

#### 7 CFR Part 46

[Docket No. FV02-369]

RIN 0581-AC21

#### Perishable Agricultural Commodities Act (PACA): Amending Regulations To Extend PACA Coverage to Fresh and Frozen Fruits and Vegetables That Are Coated or Battered

**AGENCY:** Agricultural Marketing Service, USDA.

**ACTION:** Final rule.

**SUMMARY:** The Department of Agriculture (USDA) is amending the regulations under the Perishable Agricultural Commodities Act (PACA or Act) to extend PACA coverage to include fresh and frozen fruits and vegetables that are coated or battered.

**EFFECTIVE DATE:** June 2, 2003.

**FOR FURTHER INFORMATION CONTACT:**

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**SUPPLEMENTARY INFORMATION:** This regulation is issued under authority of section 15 of the PACA (7 U.S.C. 499o).

The Perishable Agricultural Commodities Act (PACA or Act) establishes a code of fair trade practices covering the marketing of fresh and frozen fruits and vegetables in interstate and foreign commerce. The PACA protects growers, shippers, distributors, and retailers dealing in those commodities by prohibiting unfair and fraudulent trade practices. In this way, the law fosters an efficient nationwide distribution system for fresh and frozen fruits and vegetables, benefiting the whole marketing chain from farmer to consumer. USDA's Agricultural

Marketing Service (AMS) administers and enforces the PACA.

The PACA also imposes a statutory trust for the benefit of unpaid sellers or suppliers on all perishable agricultural commodities received by a commission merchant, dealer, or broker and all inventories of food or other products derived from the sale of such commodities or products. Sellers who preserve their trust rights are entitled to payment ahead of other creditors, from trust assets, of money owed on past due accounts.

In January 2000, a large food service distributor in the United States with annual net sales of approximately \$8.9 million filed for Chapter 11 bankruptcy protection. The company, which listed over \$30 million in produce debt, settled all PACA trust claims except five that involved over \$11 million in coated and battered potato products. The firm contended that the coated and battered potatoes were not covered under the PACA trust provisions [7 U.S.C. 499e(c)]. As a result of the disputed bankruptcy claims, the Frozen Potato Products Institute (FPPI), a national trade association whose members are frozen potato processors accounting for 95 percent of all frozen potato products in the United States, in June 2000, asked AMS for a written advisory opinion to clarify whether or not coated or battered potato products are covered under the PACA.

The majority of FPPI's members coat or batter their potato products to preserve their color and crispness while under heat lamps after cooking. The operation involves dipping potato strips into a mixture of water and natural vegetable starch (e.g., potato or rice). Subsequently, a crisping agent such as dextrin and/or a chemical leavening agent are added to the product. The product is then air blown to remove all but a thin layer of coating, oil-blanching, and then finally frozen.

Coated or battered products are in great demand by fast food restaurants and consumers because the operation preserves the color and crispness of potatoes held under heat lamps, a common practice in fast food restaurants, although it does not alter the taste or texture of the product. Frozen potato processors have seen dramatic growth in the market for coated potatoes since the technology was first introduced in the early 1990's,

and FPPI states that it expects that trend to continue. The food service distributor that filed for bankruptcy protection supplied approximately 36,000 restaurants throughout the United States.

According to FPPI, 8.2 billion pounds of frozen potato products were produced in the United States from April 1999 to April 2000. Out of that total, approximately 26 percent were coated or battered, accounting for 2.1 billion pounds of potato products with a market value exceeding \$800 million.

In its response to FPPI, dated August 16, 2000, AMS concluded that coating or battering does not alter the essential character of the potato products because the operation leaves them virtually indistinguishable in appearance and texture from those that have not been coated or battered. The operation, AMS stated, is directly analogous to those described in 7 CFR 46.2(u) that may be performed on a perishable agricultural commodity without changing the commodity into a food of a different kind or character. In addition, the use of starches in the operation likely has less of an impact on the texture or essential character of the potato than other processes already expressly accepted in 7 CFR 46.2(u), such as chopping, oil blanching, and adding sugar or other sweetening agents.

Although the PACA regulations previously did not specify that coated and battered perishable agricultural commodities were covered under the PACA, it has always been AMS' policy to recognize that the PACA covered such commodities since the coating or battering operation had no impact on the texture or essential character of the end product. The regulatory amendment herein codifies USDA's policy by amending the current PACA regulations' definition of "fresh fruits and fresh vegetables" [7 CFR 42(u)] to expressly extend PACA coverage to perishable agricultural commodities that have been coated or battered.

#### Comments

A proposed rule to amend the PACA regulations was published in the **Federal Register** on December 16, 2002 (67 FR 77002). The proposal sought to amend Title 7, part 46, to expressly extend PACA coverage to perishable agricultural commodities that have been coated or battered. Before the comment period ended on January 15, 2003, we