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MEMORANDUM

October 27, 2003

BY ELECTRONIC MAIL

FROM: Olsson, Frank and Weeda, P.C.

RE: Proposed Country-Of-Origin Labeling Rule

On October 30, the U.S. Department of Agriculture's Agricultural Marketing Service (AMS) will publish a proposed rule to implement a mandatory country-of-origin labeling program for certain beef, pork, lamb, fish, shellfish, peanut, fruit and vegetable products. 68 Fed. Reg. _____ (*Proposed* 7 C.F.R. Part 60). For seafood products, labels would also have to differentiate between wild and farm raised product. A copy of the proposed rule is posted on the agency's website at http://www.ams.usda.gov/cool/ls03-04prdoc.pdf. Comments must be submitted to AMS no later than ***December 29, 2003.*** In several respects, the proposed rule diverges significantly from guidelines issued by AMS last fall (*e.g.*, country-of-origin labeling would be required for certain cooked and canned products). This memorandum summarizes the proposed rule.

BACKGROUND

The Farm Security and Rural Investment Act of 2002 (Public Law 107-171, hereinafter the "2002 Farm Bill") establishes new labeling requirements for ground and whole muscle cuts of beef, pork, and lamb, as well as fish, shellfish, peanuts, and perishable agricultural commodities.[1] 7 U.S.C. § 1638 *et seq*. "Retailers", as that term is defined in the Perishable Agricultural Commodities Act, 1930 (hereinafter the "PACA") are required to inform consumers of the country of origin of a covered product. *Id*. § 1638a(a)(1). The labeling for seafood products must also distinguish between "wild fish" and "farm-raised fish". *Id.* § 1638a(a)(3). Sales of covered products must

[1] An amendment to the 2002 Farm Bill's country-of-origin labeling provisions was enacted as part of the 2002 Supplemental Appropriations Act (Public Law 107-206). This amendment clarified the qualifications for when a seafood product can be considered a product of the United States to include product caught by U.S. flagged vessels.

comply with the new labeling requirements beginning September 30, 2004. *Id*. § 1638d. The Secretary of Agriculture is required to issue regulations to implement the new labeling requirements no later than that date. *Id*. § 1638c(b).

The 2002 Farm Bill also required that USDA publish guidelines for retailers to use if they wish to implement a voluntary country-of–origin labeling program prior to the 2004 deadline. *Id*. § 1638c(a). The guidelines were published on October 11, 2002, and served as the basis for developing this proposed rule. There are, however, a number of significant differences between the guidelines and the proposed rule. In some cases, such as how AMS proposes to define a "processed food product", the proposed rule is broader in scope than the guidelines.

MAJOR CHANGES FROM VOLUNTARY GUIDELINES

There are several significant differences between the proposed rule and the guidelines issued last year. This section briefly highlights some of these differences, most of which are discussed in further detail in the following section of this memorandum.

- Scope of covered products – AMS is proposing to change the scope of coverage in two important ways.
    - First, the agency is proposing to define the term "processed food product" in a manner that may greatly expand the scope of products subject to labeling. In contrast with the guidelines, cooking or canning certain products, other than fruits and vegetables, would *not* automatically exclude it from labeling.
    - Second, AMS is excluding from coverage products that are comprised of several covered commodities (*e.g*., fruits cups, certain salad mixes, and other combination products, such as a vegetable and beef shish-kabob).
- Raw material from multiple countries – AMS is proposing that blended items comprised entirely of the same commodity (*e.g.*, ground beef) must list the countries of origin of the raw material in alphabetical order. The guidelines suggested identifying the countries in order of predominance by weight.
- Record maintenance at retail outlet – records relied upon at the point of sale (*i.e.*, the retail store) to accurately label a product would have to be retained for at least seven days after the retail sale occurs. The guidelines include a two-year record retention policy.
- Cost estimate – AMS estimates that the total record keeping cost to the entire supply chain to implement the proposed rule would be $582 million for the first year and $458 million per year after that in maintenance costs. AMS previously estimated that additional record keeping would cost $2 billion for the first year alone.

- Remotely purchased products (*e.g.*, Internet sales) – the required notice(s) may be provided at delivery. The guidelines required notice on the sales vehicle (*e.g.*, website or catalog).

PROPOSED RULE

Under the proposed rule, retailers would be required to ensure that covered commodities are labeled to indicate the country of origin. In the case of seafood, this label must also distinguish between wild fish and farm-raised fish. In accordance with the 2002 Farm Bill, food service establishments are exempt from providing labeling and processed food products are excluded from the labeling requirements.

Definition of "Retailer"

The proposed rule would define a "retailer" as "any person *licensed as a retailer* under the Perishable Agricultural Commodities Act of 1930 (7 U.S.C. 499a(b))." *Proposed* 7 C.F.R. § 60.126 (emphasis supplied). Implicit in this definition is that PACA licensure status would be used as a bright line test. Therefore, other PACA licensees that engage in occasional retail sales of covered commodities, such as foodservice wholesalers, would not be required to provide country-of-origin notification and, if appropriate, a wild/farm raised designation for their retail sales because the are not a PACA-defined "retailer". However, to the extent that these entities sell covered commodities to licensed retailers, they would still be responsible for providing the information necessary so the retailer can appropriately document the required labeling.

The agency notes that as a result of this definition, which is mandated by the 2002 Farm Bill, "the number of retailers impacted by this rule is considerably smaller than the total number of retailers nationwide." AMS estimates that there are 92,485 retail firms and 129,617 retail establishments in the U.S. that account for most sales of covered commodities, but only 4,512 firms operating 37,176 establishments are PACA-licensed retailers. *Id*. In other words, less than 30 percent of all retail establishments would be required to provide the required labeling.

Exemption for Food Service Establishments

As required by the 2002 Farm Bill, the proposed rule would exempt foodservice establishments from the new labeling requirements. *Proposed* 7 C.F.R. § 60.200(b). The regulations would define a "food service establishment" as "a restaurant, cafeteria, lunch room, food stand . . . or other similar facility . . . in the business of selling food to the public." *Id*. § 60.109. This definition includes facilities "located within retail establishments that provide ready-to-eat foods . . . ." *Id*. Accordingly, a salad bar or similar facility within a grocery store would not be required to provide labeling, but this exemption would not extend to other parts of the store.

Covered Commodities

The term "covered commodity" would be generally defined as:

- Ground and muscle cuts of beef (including veal), lamb, and pork;
- Wild and farm-raised fish and shellfish (including fillets, steaks, nuggets, and any other flesh);
- Perishable agricultural commodities as defined by the Perishable Agricultural Commodities Act, 1930 (7 U.S.C. 499a(b)); and
- Peanuts.

Proposed 7 C.F.R. § 60.106.

It is important to read these definitions in conjunction with the exclusion for processed food products. As discussed in the next section, this exclusion does not automatically extend to beef, lamb, pork, and fish products that have been cooked, seasoned, or breaded. For seafood, canned product would also not be routinely excluded. This is a major departure from the guidelines.

Exclusion for Processed Food Products

The 2002 Farm Bill excludes from the definition of covered commodities products that are an ingredient in a "processed food item." 7 U.S.C. § 1638(2)(B). As a result, country-of-origin labeling and, if necessary, a wild/farm raised designation would not be required for processed food items. *Proposed* 7 C.F.R. § 60.200(c). Since the statute does not define the term "processed food item", AMS has developed two criteria for determining when a product would be covered by this exclusion. If a product meets either of these tests, it would be considered a "processed food item".

Under the first criterion, a retail item derived from a covered commodity that has undergone a physical or chemical change causing the character of the product to be different from that of the covered commodity is deemed to be a processed food item. *Id*. § 60.121(a). Examples include oranges that have been squeezed and made into orange juice, a fresh leg of pork that has been cured and made into a ham, or flesh of a fish that has been restructured and made into a fish stick.

The second criterion covers retail items derived from a covered commodity that have been combined with either: (1) other covered commodities or (2) other substantive food components (*e.g*., chocolate, stuffing) which results in a distinct item that is not marketed as a covered commodity. *Id*. § 60.121(b). Examples include a salad mix that contains lettuce and tomatoes (but *not* different types of lettuce), peanuts in a candy bar, or a stuffed pork chop.

Importantly, this provision does not automatically exclude some products that may be commonly viewed as having undergone significant processing. While not clear from the regulatory text, the preamble notes that products such as whole muscle cuts of beef, pork, or lamb that have

been cooked, seasoned, or breaded would not be excluded from labeling as a "processed food item". Likewise, simply canning, cooking, or breading seafood would not make a product amenable to this exclusion.

Determining Country of Origin

The proposed rule would establish a detailed process for determining the country of origin of a covered commodity. The proposed standards for U.S. origin claims closely track the 2002 Farm Bill. Labeling requirements for imported products are different from the guidelines, and would not require listing all production steps that occur in countries other that the United States. Conversely, products that enter the U.S. during the production process would have to indicate the appropriate country of origin and identify the processing steps that occur in the U.S.

Commodities of U.S. Origin

Consistent with the 2002 Farm Bill, the proposed regulation would set extremely strict standards for the United States to be a product's country of origin. For beef, lamb, and pork, the product must be from animals born, raised, and slaughtered in the U.S.[2] *Id*. § 60.130(a)-(b). For farm-raised seafood, it must be hatched, raised, harvested, *and* processed in the U.S. *Id*. § 60.130(c). Wild seafood must be: (1) caught in U.S. waters or by a U.S. flagged vessel; and (2) processed in the U.S. or on a U.S. flagged vessel. *Id*. § 60.130(d). Perishable agricultural commodities and peanuts must be from products grown in the U.S. *Id*. § 60.130(e)-(f).

The proposed rule recognizes that some products that otherwise qualify for a U.S. origin claim would not automatically lose that designation if exported for further processing. *Id*. § 60.200(e)(2). For example, beef from an animal that is exclusively born, raised, and slaughtered in the U.S. would qualify for a U.S. country-of-origin designation if the carcass is further processed into steaks in a foreign country. Likewise, a potato that is grown in the U.S. but packaged in Canada would qualify for a U.S. claim. The preamble to the proposed rule cautions that a verifiable record keeping trail would be necessary, and that additional labeling may be required by other federal agencies. This situation would not apply to seafood products, as they must be processed in the U.S. in order to claim U.S. origin

Imported Products

For imported products that will not undergo further processing in the U.S., the proposed rule appears to establish a simple standard for determining the appropriate country of origin: "[I]mported covered commodities for which origin has already been established as defined by this law (*e.g*., born,

[2] For beef, a U.S. origin claim would be appropriate for animals born and raised in Alaska or Hawaii that have be transported through Canada (provided they are not in Canada for more than 60 days) and are slaughtered in the U.S.

raised, slaughtered or grown), shall retain their origin, as determined by CBP [the U.S. Bureau of Customs and Boarder Protection] at the time the product entered the United States . . . ." *Proposed* 7 C.F.R. § 60.200(f). While not explicit, this section appears address the country-of-origin labeling requirements for products imported in consumer-ready packages. Accordingly, an imported bag of frozen broccoli, for example, that is country-of-origin labeled in conformance with CBP requirements would appear to be in compliance with the proposed regulation.

Commodities Entering the U.S. During the Production Process

For beef, pork, lamb, and seafood products, the regulation would establish detailed labeling requirements for products that are imported into the U.S. for further processing. While the 2002 Farm Bill only requires country-of-origin notification, AMS is also proposing to require mandatory notification of the processing steps that occur in the U.S.

For beef, pork, and lamb, the country of origin would be the last country in which a production step occurs (*i.e.*, born, raised, slaughtered) prior to entry into the U.S. *Id*. § 60.200(g)(1). In addition to indicating the appropriate country of origin, the labeling would have to include the production steps that occur in the U.S. *Id*. For example, for an animal born and raised in Canada that is slaughtered in the U.S., would have to be labeled as "Imported from Canada, slaughtered in the U.S." While not required, the regulation allows the identification of all production steps occurring outside the U.S. if they can be substantiated. *Id*. Therefore, a label could state: "Born in country X, raised in country Y, slaughtered in the U.S."

The same general approach would be applied to imported seafood products, but the proposed regulatory text includes separate sections for "wild" and "farm-raised" seafood. *Id*. § 60.200(g)(2)-(3). However, an additional level of analysis is necessary because the term "processed" is also considered a production step for seafood products, and AMS proposes to define this term to mean any process that, pursuant to CBP policy, effectuates substantial transformation. *Id*. § 60.120. Accordingly, the country-of-origin determination for imported seafood products would turn on where the product undergoes substantial transformation prior to entering the U.S.

Blended Products

Blended items comprised entirely of the same commodity (*e.g.*, ground beef, bagged lettuce) must list the countries of origin of the raw material in alphabetical order. *Id*. § 60.200(h). This departs from the guidelines issued last fall, which required listing the countries in order of predominance by weight.

This requirement should be read carefully in conjunction with the exclusion for processed food items, which specifically excludes from labeling a covered commodity that has been mixed with other covered commodities. *Id*. § 60.121(b). The preamble attempts to highlight the differences between these two provisions. Under the discussion of what qualifies as a processed

food item, the agency notes that a fruit cup comprised of cantaloupe, honeydew, and watermelon would not have to be labeled. Conversely, a bag of red and green leaf lettuce would have to bear country-of-origin labeling, while a salad mix containing lettuce and tomatoes would not.

"Wild" or "Farm-Raised" Designation For Seafood

In addition to country of origin, the labeling of covered seafood products would have to designate whether a product is a "wild fish" or "farm-raised fish". *Id*. § 60.200(d). To qualify as "wild fish" the product would have to be "caught, taken, or harvested from non-controlled or non-select waters or beds . . . ." *Id*. § 60.134. "Farm-raised" is defined as product that has been "harvested in controlled or selected environments, *including* ocean-ranched (*e.g*., penned) fish and shellfish confined in managed beds . . . ." *Id*. § 60.108 (emphasis supplied).

Under these definitions, ocean-grown seafood that is managed in controlled environments would have to be labeled as "farm-raised". Accordingly, mussels grown in managed beds and salmon in grown in net-pens would both be "farm-raised" rather than "wild caught".

Labeling Format

The propose regulation does not include prescriptive requirements for placement or size of the country-of-origin declaration and, if appropriate, the wild/farm raised designation for seafood. The propose rule would require that the labels be "conspicuous" and placed in a location that "render[s] it likely to be read and understood by a customer . . . ." *Id*. § 60.300(b). The label may, for example, say "product of USA", or simply state the name of the country, such as "USA". *Id*. § 60.300(a). Bulk containers may contain commodities from multiple countries provided each commodity is individually labeled. *Id*. § 60.300(d). Country abbreviations, such as "U.K." for the United Kingdom, are acceptable, flags or other symbols may not be used alone, and state or similar designations are not acceptable. *Id*. § 60.300(e)-(f).

While not addressed in the proposed rule, the preamble notes that pre-approval will be necessary for country-of-origin statements on labels regulated by the Food Safety and Inspection Service (FSIS).

Record Keeping

The proposed rule would impose record keeping requirements on all segments of the food production chain -- from farmers and ranchers to retailers -- in order to substantiate the country of origin and, if applicable, wild caught/farm-raised claims. The proposal does not detail the types of records that must be maintained. In general, all records must be in English, maintained in either hard copy or electronic format, and available to USDA upon request. *Id*. § 60.400(a).

Supplier Responsibilities

All points of the supply chain prior to the retailer -- including growers, importers, distributors, handlers, packers and processors -- must make available to the next purchaser in the supply chain information about the country of origin and, if applicable, wild caught/farm-raised claims, and this information must be maintained for two years. *Id*. § 60.400(b)(1) and (3). Importantly, the entity that originates the claim (*e.g*., a meat packing facility) must have access to information to substantiate that claim. *Id*. at § 60.400(b)(1). That is, they must have in place a legally binding obligation that compels a producer or grower to provide the information necessary to substantiate any required statements.

Finally, suppliers that handle similar covered commodities from multiple countries (*e.g*., lettuce from Mexico and the U.S.) must be able to document that product is segregated and tracked in a manner that maintains the product's identity. *Id*. § 60.400(b)(5).

Retailer Responsibilities

Retailers would have to maintain information at the point of sale (*e.g*., the retail outlet) and a central facility, albeit for different periods of time at each location. At the point of sale, records relied upon to substantiate any claims must be maintained for at least seven days from the date of sale. *Id*. §60.400(c)(1). At a central facility, however, retail companies must maintain for two years records that identify supplier and other information unique to each product that substantiates the required claims. *Id*. § 60.400(c)(2).

Enforcement

With the exception of a limited discussion of enforcement activities for intermediary suppliers (*e.g*., distributors) and at the retail level, the proposed rule provides little insight into how AMS would enforce the proposed regulation. The proposed rule states that enforcement action would not be taken against a retailer if it "could not have been reasonably expected" to know of a violation based on the information provided by a supplier. *Id*. § 60.400(c)(3). A similar provision is included in the proposal to cover intermediary suppliers, such as wholesalers and other distributors. *Id*. § 60.400(b)(2). Simply put, these entities would not be held liable, for example, when their supplier provides false information and it is not possible to know of the fraud.

* * *

We trust this information is useful. If you have any questions or would like assistance in developing comments on the proposed rule, please contact Stephen Lacey at 202/518-6330 or slacey@ofwlaw.com.

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