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DEPARTMENT OF AGRICULTURE

Food and Nutrition Service

7 CFR Part 226

Child Care Food Program; Miscellaneous Amendments

AGENCY: Food and Nutrition Service, USDA.

ACTION: Final rule.

SUMMARY: This final rule makes several editorial changes and clarifications to the Child Care Food Program (CCFP) regulations. In addition, some substantive changes to those regulations are made to improve program administration. Restrictions on sponsoring organizations' use of interest bearing accounts are removed. The institution appeal process is clarified and made more flexible. Family-style meal service is presented as an option for institutions. Limitations are placed on the State agency's authority to waive certain overclaims. Certain institution responsibilities with respect to licensing and tax-exempt status are emphasized. State agencies' administrative flexibility is increased in several areas. The application of alternate approval procedures in backlog situations is rescinded. These changes will have the effect of clarifying and streamlining the CCFP.

EFFECTIVE DATE: This final rule is effective April 3, 1985.

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SUPPLEMENTARY INFORMATION:

Classification

This rule making has been reviewed in accordance with Executive Order 12291 and has not been classified as major because it will not have an annual effect on the economy of $100 million, will not cause a major increase in costs or prices, and will not have a significant economic impact on competition, employment, investment, productivity, innovation or the ability of U.S. enterprises to compete with foreign-based enterprises. This rule has also been reviewed with regard to the requirements of the Regulatory Flexibility Act (5 U.S.C. 601 et seq.). The Administrator of the Food and Nutrition Service (FNS) has certified that this rule does not have a significant economic impact on a substantial number of small entities.

In accordance with the Paperwork Reduction Act of 1980 (44 U.S.C. 3501 et seq.) the reporting or recordkeeping requirements that are included in this final rule have been submitted to the Office of Management and Budget (OMB) and have been approved under clearance 0584–0055.

Background

The CCFP is authorized by Section 17 of the National School Lunch Act (42 U.S.C. 1766). On May 13, 1983, the Department published at 48 FR 21587 a proposed rule to clarify certain aspects of the CCFP regulations, allow greater flexibility for administering agencies, and enhance Program accountability. The Department established a 60 day period during which interested parties could submit comments for the Department's consideration. During this comment period, the Department received 42 comments from FNS Regional Offices, State administering agencies, participating institutions and other interested parties. Most of the comments approved of the proposed changes. Some commentors, however, expressed disapproval or concern with some of the amendments. Other commentors suggested technical modifications to the proposed language; and some commentors requested clarification on some provisions. In addition, some commentors appeared to have misunderstood aspects of certain proposals.

In developing this final regulation, the Department considered all comments, and this preamble summarizes and discusses the significant issues raised by commentors. The Department wishes to emphasize that this preamble does not generally repeat in detail the reasons for each amendment originally proposed. Therefore, interested parties may wish to refer to the preamble of the proposed rule for a more thorough discussion of the background. For convenience, the Department will discuss the final provisions in the same order as in the preamble to the proposed rule.

1. Review Requirements

Thirty-one commentors addressed the proposal to amend § 226.6(k) to allow State agencies to reduce the number of facilities which must be visited as part of their reviews of sponsors. Of these comments, 16 were opposed; 11 were in favor; and four commented without expressing approval or disapproval. In general, opponents of this proposal believed that such reductions would impair the Program in two ways. First, State agencies would have less opportunity to learn of deficiencies which must be corrected. Secondly, the assistance which States render to providers during visits to facilities would be reduced. Two commentors apparently believed erroneously that the Department was eliminating the specific numerical requirement for performing institution reviews. Other commentors, while not necessarily disapproving of the proposal, recommended that the Department specifically require State agencies to reallocate any resources that may be available due to these reductions. Finally, some commentors found the proposed formulas to be overly complicated.

The Department initially proposed this provision in the belief that the number of facilities which State agencies must review as part of their review of a sponsoring organization might be reduced without impairing program accountability or assistance. In view of the concerns expressed by commentors, the Department has reconsidered this action. The significant reductions under the proposal would have occurred with respect to sponsors of large numbers of facilities (e.g., sponsors with over 200 homes or 25 centers). Consequently, few State agencies would have realized any significant change in their administrative responsibilities. Moreover, while States with large sponsors would have had their review requirements reduced somewhat, the Department's recent experiences with some larger sponsors suggest that a relaxation of review activity would not be in the best interests of the Program at this time. For these reasons, the Department has withdrawn the proposal.

The Department also proposed to amend § 226.6(k) to replace the list of program areas to be reviewed with a more general requirement that in conducting program reviews State agencies assess compliance with the CCFP regulations and applicable instructions. Four commentors approved of this change, while nine disapproved. Those disapproving generally maintained that all CCFP reviews should adhere to the same standards nationwide. There was some concern that the proposed amendment could lead to relaxation of standards on the one hand and harassment of institutions and facilities on the other.

The Department proposed this amendment in order to conform the CCFP to other FNS programs. It should be noted that specific review standards are not included in the existing CCFP provisions; there is only a list of general Program areas to be reviewed. Since in any case State agencies, institutions and facilities are responsible for meeting all requirements set forth in the CCFP regulations and instructions, the Department does not consider that the proposed amendment will result in decreased accountability or harassment of institutions and facilities. Therefore, the Department is adopting the proposed change.

The Department received 30 comments on the proposal to amend §226.16(d)(4)(ii) to permit sponsors of day care homes to make an *average* of three visits per home each year in certain circumstances, rather than requiring *each* home to be visited three times per year. Eleven commentors approved of the proposal, while 19 disapproved. The Department believes, however, that many disapproving commentors misunderstood the nature of the proposed change. Many of those who disapproved appeared to believe that the Department was reducing the overall monitoring requirement for sponsoring organizations.

However, sponsors will perform just as many total annual reviews under the proposed system as they must currently perform. For example, if a sponsor operates 100 day care homes, that sponsor must perform a minimum of 300 annual visits regardless of whether each home is visited three times or an *average* of three visits per home is made each year. The only change is that sponsors can vary the number of annual visits to individual homes to allow for a greater number of visits to homes that need additional guidance and a lesser number of visits to homes with fewer deficiencies.

The Department also wishes to emphasize that sponsors may not exercise this option unless the State agency approves and FNS concurs with the approval. As stated in the preamble to the proposed rule, approval of a request to exercise this option will be based on a finding that the sponsor will be able to allocate its resources more efficiently and to provide better assistance where it is most needed. Approval would not be granted, for example, merely to enable a sponsor to reduce its travel expenses associated with monitoring. It should also be noted that State agencies are not required to permit this option. Moreover, those State agencies which do permit the option may only give approval on a case-by-case basis. In any case, at the minimum each day care home must be reviewed twice per year. For these reasons, the Department does not consider that this option will lead to reduced oversight of day care homes. Finally, one commentor suggested that the Department should modify its requirement that not longer than six months elapse between home reviews.

However, the Department considers that the six-month requirement will be increasingly important for any homes that may be visited only twice a year. Therefore, the proposed rule is adopted without relaxing the requirement that not more than six months elapse between reviews.

2. Interest-Bearing Accounts

Twenty commentors addressed the proposal to delete the provision requiring sponsors to maintain Program payments in non-interest bearing accounts for the period between receipt and disbursement. Thirteen commentors (representing State agencies, FNS Regional Offices, institutions and other interested parties) approved of the proposed rule. Four commentors disapproved, and three parties commented on aspects of the proposal without expressing clear-cut approval or disapproval. As the Department noted in the preamble to the proposed rule, § 3015.46 of the Department's Uniform Federal Assistance Regulations (7 CFR Part 3015) exempts State agencies and their subrecipients (i.e. sponsors, institutions and child care facilities) from the general rule requiring the return of interest earned on advances to the Federal government. Deleting the provision on non-interest bearing accounts allows sponsors to earn interest on advances of Program funds and brings the CCFP regulations into conformity with 7 CFR Part 3015.

In the absence of any Federal restriction, State law and policy governs the use of interest earned by sponsors, institutions and child care facilities on advances of Program funds, unless they are in a program directly administered by FNS. These final regulations amend § 226.7(i) to require State agencies to maintain a statement of the State's law and policy on file. In the States where FNS administers the CCFP directly, interest earned on advances must be returned to FNS, as required by the general rule of 7 CFR 3015.46(a).

Those commentors who disapproved of the proposal were generally concerned that institutions located in some States might benefit from laws which are less stringent than those of other States or the Federal government. However, the Department does not believe that a nationwide requirement would be consistent with 7 CFR Part 3015. States are free to regulate this matter. For this reason, the Department is deleting this provision as provided in the proposed rule. However, States are reminded that 7 CFR Part 3015 instructs them to minimize the time between the disbursement of advances to a recipient and the recipient's need for such monies.

3. Appeals Procedures

The Department proposed six amendments to the institution appeal process in § 226.6(j). First, the State agency would be permitted to be represented at hearings, and as a result, a second proposal would require that the State agency, as well as the appellant, be given 10 days notice of the time and place of the hearing. The third proposal was that institutions would receive no reimbursement for meals served during an appeal of a termination unless they win the appeal. Fourth, the Department proposed to allow State agencies to use their own appeals procedures rather than the CCFP procedures under certain conditions. The fifth proposal would require State agencies to advise institutions of the full appeal process at least once each year, rather than requiring a full description with each notice of an adverse action. Finally, the Department reiterated that State agencies would be accountable for claims based on Federal audits even if a State appeals officer held that the institution was not liable.

There was no disagreement with the proposals to amend § 226.6(j)(3) and (4) to ensure that the State agency has the opportunity to be represented at hearings. These proposed amendments, therefore, are being adopted for the reasons stated in the preamble accompanying the proposal.

Commentors tended to be evenly divided on the other proposals. These provisions are discussed below.

The Department proposed an amendment to § 226.6(j)(9) to reimburse institutions for meals served during an appeal of a termination action only if their appeal is successful. Eleven commentors approved of this proposal, and ten disapproved. In general, those who disapproved were concerned that this policy might discourage institutions from either exercising their right to an appeal or from continuing to serve meals which meet CCFP requirements pending a decision on the appeal. Some commentors noted that institutions are sometimes terminated, not for fraud or health violations, but for cash flow problems. Consequently, there were suggestions for modifying this provision to allow institutions to receive continuous reimbursement if the termination action is for mismanagement of funds but to apply the proposed provision if the termination action is for meal pattern violations. Also, one commentor who basically approved of the proposal suggested a modification for sponsors of homes, whereby operating reimbursement for home providers would continue to be paid regardless of the outcome of the appeal, while administrative reimbursement would be paid only if the sponsor wins its appeal.

As the Department noted in the preamble to the proposed rule, termination actions are taken on the basis of serious deficiencies, generally involving financial mismanagement or fraud. Therefore, unless a review officer determines that the State agency's action in terminating the sponsor was improper, the Department does not believe terminated institutions should continue to receive funds. The Department wishes to emphasize that terminations are the result of *serious* problems. Cash flow difficulties, for example, may be the symptom of underlying management deficiencies and cannot be automatically treated as minor. Moreover, the Department does not believe that the proposed rule would limit an institution's access to an appeal. This policy is in effect in the Summer Food Service Program. The Department is not aware that it has resulted in a diminished number of sponsors pursuing their appeal rights.

The Department also does not concur with commentors' recommendations for the alternate procedures discussed above. Fiscal mismanagement is a serious problem. If the institution in question were to continue to receive reimbursement for meals served regardless of the outcome of the appeal, the State agency would have to either increase its monitoring during the period of the appeal to assure itself of proper management, or risk having to lodge an overclaim against the institution after the appeal. In either event, the administrative cost and complexity would be increased for the State agency without providing additional protection for improperly terminated institutions. Consequently, the Department is adopting this amendment as proposed.

Twenty commentors addressed the proposal to allow State agencies to use their own appeal procedures as long as these procedures conform to certain criteria. Eleven commentors approved of the proposed changes, and nine disapproved. Those who disapproved tended to be concerned that this action might afford institutions less protection than they currently enjoy under the CCFP regulations. Some commentors asserted that the CCFP, as a Federal program, must have a uniform appeals procedure. One commentor suggested that this amendment could permit State agencies to vary their procedures from one institution to another. Finally, one party appeared to believe that the Department was proposing to delete the list of appealable actions currently included in this passage.

The Department does not believe the proposed amendment would result in less protection for institutions. This change was proposed to alleviate those situations in which review officials must follow CCFP guidelines despite the fact that the State has procedures which are followed for appeals in other programs. The Department believes that the criteria which must be met by State appeal procedures will ensure the rights of appellants. It should also be noted that most of the differences between CCFP and State appeal procedures involve time limits for accomplishing certain actions. Essential protections such as the right to a review or hearing, the right to counsel and the right to an impartial review officer are required to be a part of the State procedure substituted for the CCFP system. Moreover, since all appeals must be decided on the basis of the Program regulations and instructions, the uniformity of Program policy will not be undermined. The only change will be in the area of non-substantive appeal procedures. The final rule has been amended to make it clear that State agencies must apply the same procedures to all appellants in the State. Finally, the amendatory directions clearly state that the proposed language replaces only the last sentence of Paragraph (j). The first sentence, which lists appealable actions, has not been altered. In response to one comment, however, the Department is establishing a time limit of 120 days for the entire appeal process to be completed. The Department believes this modification will ensure a speedy review while still allowing flexibility for State agencies. For these reasons, the Department is adopting this amendment.

Commentors were also divided on the proposal to require State agencies to advise institutions of the appeal procedures only once each year. Eleven commentors approved, and seven disapproved of this provision. As the Department stated in the preamble to the proposed rule, State agencies will still be required to advise institutions of their right to appeal each time an appealable action is taken. The intent of the proposal was to remove the burden of decribing the entire appeals procedure each time an adverse action is taken. Some commentors objected to the proposal on the grounds that participants might forego their appeal rights if they are not aware of the procedures for an appeal. The Department wishes to emphasize, however, that the procedures for filing appeals must still be made available to institutions at least once each year. Further, in response to a comment, the Department is adopting the language of the Summer Food Service Program regulations, which require State agencies to provide this information each year when the institution's application for participation in the Program is received. Moreover, the final rule has been amended to provide that this information must be provided at other times during the year to institutions who request it. Therefore, the Department is adopting this amendment, with the changes noted.

Finally, the Department proposed to add a paragraph (j)(12) to clarify the Department's policy that State agencies are liable for overclaims established in Federal audits, even though a State review officer dismisses the overclaim against the institution(s) involved. The Department received 15 comments on this provision, with seven commentors approving and eight disapproving. Those who disapproved tended to believe that it would be unfair to hold State agencies liable for overclaims if the State agency is not able to collect the money from the institution. Commentors were concerned, moreover, that if this situation did exist, review officers may not be free to render an impartial decision. Finally, some commentors suggested that in order to implement this provision, the Department must establish an appeal system for Federal audits.

Once a Federal claim has been established against a State agency based on Federal audit findings, only the Department has the authority to adjust, settle, compromise or deny that claim. The actions of State review officers cannot, therefore, overrule the findings of an audit. The Department does not believe that this provision will result in unfair decisions against institutions that are appealing Federal audit findings. This provision emphasizes the policy which is already in effect, although perhaps not currently understood. Review officers have traditionally been characterized by impartiality, and the Department expects this pattern to continue.

Further, the Department does not agree that this provision is necessarily unfair to State agencies. There are situations in which the State agency, rather than the institution, is responsible for an overclaim cited in a audit. For example, if the violation of Program requirements giving rise to the claim occurred because of improper guidance provided by the State agency, a review officer could properly rule that the institution did not have to repay the State agency for the loss. In such a situation, the State agency is responsible for the action giving rise to the audit claim and the Department can assert the overclaim against the State agency pursuant to § 226.14(c).

Finally, although there is no formal appeal mechanism for Federal audits, the Department believes the audit closure process affords ample opportunity for a just determination of audit findings. Before audit findings become final, representatives of the Office of the Inspector General, FNS and the State agency meet to discuss preliminary findings and recommendations. During this phase of the audit process, the State agency reviews all findings and evidence and presents its own documentation for any findings it believes to be erroneous. A final audit report is issued only after this phase has been completed. Because this process assures the State agency of the right to comment on findings and to present evidence in its behalf, the Department does not consider that an additional level of hearings is needed. For these reasons, the Department is adopting this provision as proposed.

4. Audit Disregard

Fifteen commentors addressed the proposal to allow FNS or the Office of the Insepctor General to disregard an overpayment which does not exceed $100. All fifteen approved of this increase. Some commentors, in fact, suggested an ever higher disregard limit. The Department proposed this increase from the former $35 limit because it is not cost effective to pursue overpayments of less than $100. The Department does not consider, however, that the limit could be further increased at this time without sacrificing accountability. The proposed amendment to § 226.8(e) has been modified slightly to make clear that the language allowing State agencies to disregard certain overpayments refers to overpayments identified in State agency sponsored audits. FNSROs which act as State agencies may disregard overpayments less than $100, while State agencies in State administered programs must follow State law on the subject. It was brought to the Department's attention, however, that the word "any" had been inadvertently omitted from immediately before the word "overpayment" in the proposed rule. Therefore, this word has been restored in the final rule.

5. Meal Requirements

The Department received 12 comments on the proposed clarifications to the snack requirements in § 226.20(a)(3) and § 226.20(d)(2). Sixteen commentors addressed the addition of § 226.20(o), which clarifies that family-style meal service may be employed by institutions. All comments on all three proposals were favorable. Some commentors did suggest that the regulations should outline specific requirements for family-style meals. However, the Department believes such details are more appropriate to guidance materials. Therefore, these three amendments are adopted as proposed.

6. Waiver of Claims

The Department proposed to amend § 226.14(b) to stipulate that State agencies may not accept corrective action in lieu of collection of overpayments for meal pattern violations by institutions which prepare their own meals if the overpayment has been established by a Federal audit. Seven commentors approved of this provision; two disapproved; and two commented on the general desirability of accepting corrective action in such situations.

One disapproving commentor believes that losses of less than $100 should be disregarded. The other questioned the extension of this policy to situations in which an overclaim based on a Federal audit has been dismissed by a State review officer. One approving commentor also stipulated that institutions must be allowed to appeal overclaims. The Department wishes to emphasize that this limitation applies only to claims arising out of Federal audits. As noted in the discussion on appeals, overclaims established by Federal audits may not be waived by State agencies under any circumstances. The Department believes it is consistent with this limitation to require State agencies to pursue collection efforts for all overclaims, as the State agency will be held accountable for any uncollected amounts unless FNS and the Office of the Inspector General waive the loss. As clarified in the new paragraph (j)(11) of § 226.6, this accountability extends to situations in which a claim based on a Federal audit against an institution has been dismissed by a review officer. State agencies continue to have the latitude to accept corrective action in lieu of pursuing overclaim established by means other than Federal audits. For these reasons, this amendment is adopted as proposed.

7. Eligibility Requirements

The Department proposed two amendments which affect institutions' eligibility. The first of these, § 226.6(d)(1)(i) addressed the continued CCFP eligibility of institutions admitted to the CCFP on the basis of participation in another Federal program. The proposal would require those institutions admitted to the other Federal programs on the basis of having valid licenses to maintain those licenses in order to continue to be eligible for the CCFP. This proposal received overwhelming approval from commentors. Seventeen commentors approved, while only two disapproved. The Department noted, however, that approving and disapproving commentors alike appeared to misunderstand the extent to which the proposed amendment would apply. Many commentors believed the proposal would adherence to licensing standards as an absolute condition of eligibility for institutions admitted into the CCFP on the basis of participation in another Federal program. Consequently, opposing commentors were concerned that many safe, well-operated Head Start establishments in their States might be forced out of the CCFP because they were note licensed child care centers. Because of the apparent misunderstanding, the Department wishes to reiterate the application the application and intent of this provision.

By law, facilities which have been approved for another Federal program, primarily Head Start, are eligible to participate in the CCFP as well.

regardless of whether or not they are licensed by State or local authorities.

This consideration is based on the fact that institutions must meet certain performance standards to be admitted to Head Start, and these standards require participants to obtain State or local licensing, where available. If licensing is not available, Head Start applies its own facility standards. The proposed provision would *not* apply to facilities admitted under Head Start's own standards. It has happened, however, that facilities admitted to Head Start on the basis of licenses have occasionally continued to participate in Head Start after having lost their licenses. Since these facilities had not yet been terminated from Head Start, they maintained that they were still eligible to participate in the CCFP. This situation clearly has the potential of permitting participation by institutions whose environments may be detrimental to the health and safety of enrolled children, and the Department believes that it has an obligation to ensure that Program benefits are made available only to institutions which offer high quality child care.

For this reason, the Department proposed that institutions admitted to a Federal program such as Head Start on the basis of licensing would not be eligible for the CCFP if they lose their licenses, even if they have not yet been terminated from that program. In reviewing the preamble to the proposed rule, the Department considers that commentors may have misunderstood the Department's intent. However, the Department does not believe it is necessary to repropose this amendment. The only disapproving commentors were those who thought the proposal could result in the disqualification from the CCFP of numerous high quality Head Start facilities which, for one reason or another, are not licensed. The Department again wishes to provide assurance that licensing is not a condition of CCFP eligibility for these institutions unless it was the basis for admission to Head Start. Approving commentors agreed with the general principle of the amendment. Therefore, the Department is adopting the proposed amendment with language changes to clarify the intent of this passage.

The Department also proposed to amend § 226.15(a) to clarify that the institution, not the State agency, is responsible for documenting compliance with Internal Revenue Service (IRS) requirements when it has been allowed to participate in the CCFP on the basis that it is moving toward obtaining tax-exempt status. Twelve commentors approved of the proposal; one disapproved; and one raised some questions without expressing clear approval or disapproval. Some commentors, while approving of the provision, suggested shortening the length of time an institution can remain on the Program while awaiting IRS approval. Additionally, some commentors requested further clarification on whether institutions in this category could participate for longer than 12 months pending IRS approval of tax-exempt status, and some questions were raised about appeal rights. The Department wishes to emphasize that no change was proposed to this paragraph other than to add the sentence specifying that documentation of compliance with IRS requirements is the institution's responsibility. The Department is not contemplating any further changes to the procedures outlined in this paragraph. State agencies will continue to observe the time limits currently established, and institutions will continue to enjoy the current appeal rights. Therefore, the Department is adopting this amendment as proposed.

8. Administrative Flexibility/Program Simplification

a. *Readmission of seriously deficient institutions.* Nine commentors approved of the Department's proposal to amend § 226.6(c) by deleting the reference to a three year waiting period for readmission of institutions which have been found to be seriously deficient in their operation of any Federal child nutrition program. Two commentors disapproved on the grounds that State agencies would be able to deny readmission indefinitely even though the institution has corrected its deficiencies. These commentors recommended that the passage be revised to require the immediate readmission of institutions which have taken corrective action. The Department wishes to point out that the proposed amendment places the emphasis on corrective action as a precondition of readmission to the Program. However, all other Program requirements must still be met before an institution can be readmitted. Therefore, the Department is adopting the amendment as proposed. The Department also notes that the proposed rulemaking established an inconsistency by not also deleting the three year waiting period for entering into agreements with any institution which had, in the past, been seriously deficient in its operation of one or more child nutrition programs. The Department did not intend this inconsistency. Therefore, this final rule further revises this paragraph to clarify the policy that corrective action is a precondition of approval for any institution which has experienced serious deficiencies.

b. *Health/sanitation and fire/safety inspections.* The Department proposed to define a "current" health, fire or safety permit as one issued within the past 36 months, rather than the past 12 months as presently required under § 226.6(d)(2)(i)(C)*(1)* and *(2)*. This proposal was intended to alleviate the difficulties some jurisdictions experience in attempting to obtain annual inspections. Of 22 comments received on this proposal, 16 disapproved, representing all quarters of the Program. In general, commentors acknowledged that annual permits are occasionally difficult to obtain; nevertheless, the consensus was that the proposed change could be detrimental to the health and safety of children participating in the CCFP. In view of this widespread concern, the Department is withdrawing this proposed amendment.

c. *Commodities/cash-in-lieu of commodities.* Nine commentors approved of the proposed amendment to § 226.6(g), deleting the provision permitting institutions to request a switch from commodities to cash-in-lieu or vice versa during the school year. One commentor disapproved, and one commentor recommended an additional restriction. The disapproving commentor expressed concern that by requiring institutions to elect to receive commodities at the start of the school year, they might not receive the full value of cash-in-lieu because there can be a lack of variety of available foods at that time of the year. While the variety may be limited in July, over the course of the year an ample variety of foods will be available to institutions. One commentor, while not disapproving of the proposal, recommended that no institution, newly admitted or otherwise, should be allowed to elect to receive commodities after June 1. However, the statutes governing the program require that all institutions be accorded the opportunity to receive commodities, except in limited situations. Moreover, the administrative burden is not primarily caused by institutions which are admitted to the program after June 1, but by institutions which desire to change their decision after the State distribution agency has acted. For these reasons, the Department is adopting this provision as proposed.

d. *Corrective action plans.* Thirteen commentors responded to the proposal to modify § 226.7(c) by adding a good cause exception to the 60-day time limit for State agencies to submit corrective action plans. Ten commentors approved, and three disapproved. In general, those who disapproved believed State agencies should be held to standards for corrective action as stringent as those imposed on institutions. It was also suggested that delays by the State agency in accomplishing corrective action could be detrimental to participating institutions in the State. The Department believes, however, that correcting deficiencies at the State level often involves more planning time and deals with more complex issues than at the institution level. It will frequently be necessary for the State agency to receive commitments for funding and staff or to coordinate activities with other agencies of the State in order to deal effectively with many deficiencies. Consequently, the Department continues to believe that development of an effective plan will sometimes require longer than 60 days and that a good cause exception should apply in these instances. The Department wishes to emphasize that it has no intention of relaxing its requirements for corrective action. The amendment merely allows FNS and State agencies to exercise greater flexibility in developing a workable plan and does not affect timeframes for the actual completion of the corrective action. For these reasons, the Department is adopting the provision as proposed.

e. *Sponsor/home agreements.* The Department proposed two amendments dealing with agreements between sponsoring organizations and their day care homes. The first proposal would amend § 226.18(b) to allow State agencies the option of either developing these agreements themselves or requiring their sponsors to formulate their own agreements, subject to State agency approval. Ten commentors approved of this proposal, and five disapproved. Those who disapproved noted that this proposal could increase the administrative burden both for sponsors, who would be responsible for developing the agreements, and State agencies, who would have to review them. In proposing this amendment, the Department intended to increase flexibility and reduce burden by permitting State agencies the option of allowing sponsors which have developed their own agreements to use them, as long as all CCFP requirements were included. State agencies would not, however, be required to extend this consideration to their sponsors. The decision to do so is entirely a State agency option. The Department agrees, however, that it would be unfair for State agencies to require sponsors to develop their own agreement. Such a requirement would be especially burdensome for very small sponsors that lack the resources to develop and print their own forms. Therefore, the Department is modifying the proposed amendment to allow State agencies to approve sponsors' requests to use their own agreements as long as all CCFP requirements are included. The Department is also incorporating this amendment in §226.6(n). The proposed rule excluded this conforming amendment through oversight, and the Department is correcting this omission in the final rule.

The Department also proposed to amend § 226.18(b)(8) to allow State agencies to stipulate limits or procedures for terminations of agreements between sponsors and day care homes for convenience. Ten commentors approved of the proposal, while three disapproved. One State agency was concerned that the proposal could interject State agencies into disputes between sponsors and day care homes by requiring the State agency to determine whether there was sufficient cause for termination. Another disapproving commentor was concerned that the proposal could limit the ability of sponsors to deal with homes which may be violating program requirements. The third opposing commentor was concerned that this provision might enable State agencies to confer monopolies upon selected sponsors. The Department emphasizes that any limitation would be at the State agency's option. State agencies are not required to act in this area. Secondly, the revision does not affect the right of either party to terminate the agreement for cause, which would include instances of program violations. Finally, since agreements are effective only for one year, it is not possible to employ this provision as a means of restricting competition among sponsoring organizations. Therefore, the Department is adopting the amendment as proposed.

f. *Alternate approval in backlog situations.* Eleven commentors addressed the proposal to delete § 226.6(b)(4), which permits State agencies to employ alternate procedures for approving child care centers, outside-school-hours centers and day care homes which have not been previously licensed in situations of backlogs at the licensing agency. Nine commentors approved; one disapproved; and one requested some additional clarification. The one disapproving commentor believed that rescission of alternate approval in these backlog situations may create delays in participation for some providers. The Department does not consider, however, that this effect would be widespread. Moreover, as the Department noted in the preamble to the proposed rule, this provision has created a significant administrative burden for State agencies and has placed State agencies in the untenable position of deciding on the adequacy of facilities when an official licensing agency is available. The Department continues to believe that this responsibility should rest solely with licensing agencies when they exist. One commentor also asked whether or not this elimination of the backlog provision would extend to institutions which are reapplying but have not yet had their licenses officially renewed. The backlog provision in § 226.6(d)(4) was never intended to apply to license renewal situations. In cases in which licensing is available, § 226.6(d)(1) requires the State agency to ensure only that child care centers, outside-school-hours centers and day care homes are either licensed or complying with procedures to renew licensing in situations where the State agency has no information that licensing or approval will be denied. For these reasons, the Department is adopting the proposal to delete this provision. The final regulation also adopts the proposal to delete the reference to this provision in § 226.6(d)(3)(iii) and § 226.6(m).

9. Clarifications/Editorial Changes

The Department proposed two editorial amendments. The first of these specified in § 226.6(m) that institutions are responsible for ensuring that all deficiencies identified during reviews are corrected. The Department proposed this minor change to clarify that institutions have the primary responsibility for maintaining compliance with child care standards. Eight commentors approved of this amendment, and one disapproved. It appears, however, that the one disapproving commentor may have misunderstood the nature of the amendment. The commentor was concerned that the Department was requiring State agencies to review against licensing standards. The amendment merely adds the clause at the end of the first sentence specifying that "the institution shall ensure that all violations are corrected." The remainder of the sentence was unchanged. It should be noted, moreover, that the State agency's review responsibilities in this passage extend only to facilities admitted to the Program under the alternate approval provisions of

§ 226.6(d)(3). Therefore, the Department is adopting this amendment as proposed. The Department does wish to emphasize, however, that ultimate responsibility for compliance with this provision rests with the State agency, and language to this effect has been inserted in the regulation.

The second editorial amendment was to streamline the regulations by deleting the list of items in § 226.6(b) which are required to be considered during the application approval process. Eight commentors approved, and three disapproved. The disapprovals were based on the fact that this provision is not entirely duplicated by a similar provision in § 226.6(e), contrary to the statement made in the preamble to the proposed rule. Consequently, these commentors believed State agencies might not have sufficient guidance on what to consider in approving applications. The Department regrets having made this error in the preamble and agrees that deletion of this list could leave State agencies with insufficient direction with respect to certain annual requirements. Therefore, the Department is withdrawing the proposal to delete these items from the regulations.

10. State Agency Review Systems

Although no specific amendment was proposed, the Department solicited comments on the question of whether or not State agencies should be permitted to substitute their own review systems for the review requirements of § 226.6(k), provided FNS approved of the State agency's system. The intent of any such amendment would be to allow a certain degree of flexibility with respect to frequency of review when the State agency could demonstrate good cause.

Commentors were fairly evenly divided, with six (mostly States) approving of the change and four (mostly institutions) disapproving. Those disapproving were generally concerned with the possibility that State agencies might depart from the Program standards set forth in the regulations. The Department wishes to reiterate, however, that any such proposal would be directed specifically at review systems and issues such as determining standards for frequency of reviews or methods of selecting institutions for review. The reviews would still have to assess compliance with program regulations. The Department is taking all comments under consideration.

List of Subjects in 7 CFR Part 226

Day care, Food assistance programs, Grant programs-health, Infants and children, Reporting and recordkeeping requirements, Surplus agricultural commodities.

Accordingly, Part 226 is being amended as follows:

1. In § 226.6, by revising the first three sentences of the introductory text of paragraph (c); revising paragraph (d)(1)(i); revising the second sentence of (d)(3); removing paragraph (d)(4); revising paragraph (g); adding two sentences after the first sentence and revising the last sentence of the introductory text of (j); revising the second sentence of paragraph (j)(1); revising the last sentence and adding a new sentence at the end of (j)(3); revising paragraph (j)(4); placing a period after the word "action," in the third sentence; removing the word "and," and adding a sentence at the end of paragraph (j)(9); adding paragraph (j)(12); revising the third sentence of paragraph (k); revising the first and fourth sentences of paragraph (m); and adding a new sentence between the first and second sentence of paragraph (n) to read as follows:

§ 226.6 State agency administrative responsibilities.

* * * * *

(c) *Denial of applications and termination of institutions.* The State agency shall not enter into an agreement with any applicant institution identifiable through its corporate organization, officers, employees, or otherwise, as an institution which participated in any Federal child nutrition program at any time and which was seriously deficient in its operation of any such program unless the deficiencies have been corrected to the satisfaction of the State agency, with FNS concurrence. The State agency shall terminate the program agreement with any institution which it determines to be seriously deficient. Following such termination, the institution shall not be eligible to participate in the program until such time as the State agency, with FNS concurrence, determines that the institution has taken appropriate corrective actions to prevent recurrence of the deficiencies that led to a termination from the program. * * *

(d) *Licensing/Approval.* * * *

(1) *General.* * * *

(i) Are licensed or approved by Federal, State, or local authorities, provided that institutions which are approved for Federal programs on the basis of State or local licensing shall not be eligible for the Child Care Food Program if their licenses lapse or are terminated; or

* * * * *

(3) * * * Licensing or approval is not available when (i) no Federal, State, or local licensing/approval standards have been established for child care centers, outside-school-hours care centers, or day care homes; or (ii) no mechanism exists to determine compliance with licensing/approval standards. * * *

* * * * *

(g) *Commodity distribution.* The State shall annually inquire as to the preference of each institution for commodities or cash-in-lieu of commodities. Each institution electing cash-in-lieu of commodities shall receive such payments. Each institution which elects to receive commodities shall have commodities provided to it unless the State agency, after consultation with the State commodity distribution agency, demonstrates to FNS that distribution of commodities to the number of such institutions would be impracticable. The State agency may then, with the concurrence of FNS, provide cash-in-lieu of commodities for all institutions. A State agency request for cash-in-lieu of all commodities shall be submitted to FNS not later than May 1 of the school year preceding the school year for which the request is made. The State agency shall, by June 1 of each year, submit a list of institutions which have elected to receive commodities to the State commodity distribution agency, unless FNS has approved a request for cash-in-lieu of commodities for all institutions. The list shall be accompanied by information on the average daily number of lunches and suppers to be served to children by each such institution.

* * * * *

(j) *Institution appeal procedures.* * * * State agencies may use their own State appeal procedures provided the same procedures are applied to all appellants in the State and the procedures meet the following requirements: appellants are assured of a fair and impartial hearing before an independent official at which they may be represented by legal counsel; decisions are rendered in a timely manner not to exceed 120 days from the date of the receipt of the request for review; appellants are afforded the right to either a review of the record with the right to file written information, or a hearing which they may attend in person; and adequate notice is given of the place, date and procedures of the hearing. The appeal procedures adopted by the State agency shall be made available in writing each year to all institutions at the time of application for participation in the Program and upon request. If the State has not established its own appeal procedures or the procedures do not meet the above listed criteria, the State agency shall observe the following procedures at a minimum:

(1) * * * The notice of action, which shall be sent by certified mail, return receipt requested, shall also include a statement indicating that the institution has the right to appeal the action;

* * * * *

(3) * * * Failure of the appellant institution's representative to appear at a scheduled hearing shall constitute the appellant institution's waiver of the right to a personal appearance before the review official, unless the review official agrees to reschedule the hearing. A representative of the State agency shall be allowed to attend the hearing to respond to the appellant's testimony and to answer questions posed by the review official;

(4) If the appellant has requested a hearing, the appellant and the State agency shall be provided with at least 10 calendar days advance written notice, sent by certified mail, return receipt requested, of the time and place of the hearing;

* * * * *

(9) * * * If the institution or facility has been terminated for this reason, the State agency shall so specify in its notice of action. Institutions electing to continue operating while appealing terminations shall not be reimbursed for any meals served during the period of the appeal if the State agency's action is upheld; and

* * * * *

(12) In cases where an appeal results in the dismissal of a claim against an institution which was asserted by the State agency based upon Federal audit findings, FNS may assert a claim against the State agency in accordance with the procedures outlined in § 226.14(c).

(k) *Program Assistance.* * * * Program reviews shall assess institutional compliance with the provisions of this Part and with any applicable instructions of FNS and the Department. * * *

* * * * *

(m) *Child Care Standards Compliance.* The State agency shall, when conducting administrative reviews of child care centers, outside-school-hours care centers, and day care homes approved by the State agency under paragraph (d)(3) of this section, determine compliance with the child care standards used to establish eligibility, and the institution shall ensure that all violations are corrected and the State shall ensure that the institution has corrected all violations. * * * If, during an administrative review of a child care center, outside-school-hours care center, or day care home not approved by the State agency under paragraph (d)(3) of this section, the State agency observes violations of applicable health, safety, or staff-child ratio standards, or attendance in excess of licensed capacity, the State agency shall promptly refer such violations to the appropriate authority. * * *

(n) * * * However, the State agency may, at the request of the sponsor, approve an agreement developed by the sponsor. * * *

2. In § 226.7, paragraph (c), a new sentence is added between the second and third sentences, and in paragraph (i) a new sentence is added to the end of the text to read as follows:

§ 226.7 State agency responsibilities for financial management.

* * * * *

(c) *Management Evaluations and Audits.* * * * If a State agency makes a showing of good cause, however, FNS may allow more than 60 days in which to submit a plan. * * *

* * * * *

(i) * * * The State agency shall maintain on file a statement of the State's law and policy governing the use of interest earned on advance funds by sponsors, institutions and child care facilities.

* * * * *

3. In § 226.8(e), revising the first sentence to read as follows:

§ 226.8 Audits.

* * * * *

(e) In conducting management evaluations or audits for any fiscal year, FNS or OIG may disregard any overpayment which does not exceed $100. In conducting State agency sponsored audits in State administered programs, the State agency may disregard any overpayment which does not exceed the amount established by State law, regulations or procedures as a minimum for which claims will be made for State losses generally. * * *

* * * * *

4. § 226.14 is amended by adding a new sentence to the end of paragraph (b), to read as follows:

§ 226.14 Claims against institutions.

* * * * *

(b) * * * However, the State agency shall not disregard any overpayments or waive collection action arising from the findings of Federal audits.

* * * * *

5. § 226.15, paragraph (a) is amended by adding a new sentence between the second and third sentence to read as follows:

§ 226.15 Institution provisions.

(a) *Tax-exempt status.* * * * It shall, however, be the responsibility of the institution to document that it has complied with all requirements of IRS and has provided all information requested. * * *

* * * * *

6. § 226.16, paragraph (d)(4)(ii) is revised to read as follows; paragraph (j) is removed, and paragraph (k) is redesignated as paragraph (j).

§ 226.16 Sponsoring organization provisions.

* * * * *

(d) * * *

(4) * * *

(ii) Three times each year at each day care home, provided at least one review is made during each day care home's first four weeks of Program operations and not more than six months elapse between reviews. However, based on case-by-case findings by the State agency that improved efficiency and more effective management will result and subject to FNSRO approval, State agencies may allow some or all of their sponsors to conduct reviews an average of three times each year per day care home, provided that each day care home is reviewed at least twice each year, at least one review is made during each day care home's first four weeks of Program operations, and no more than six months elapse between reviews; and

* * * * *

7. In § 226.18, the second sentence of paragraph (b) is revised and a new sentence after the second sentence has been added; and paragraph (b)(8) is revised to read as follows:

§ 226.18 Day care home provisions.

* * * * *

(b) * * * Sponsoring organizations shall enter into a written agreement with each sponsored day care home which specifies the rights and responsibilities of both parties. This agreement shall be developed by the State agency, unless the State agency elects, at the request of the sponsor, to approve an agreement developed by the sponsor. At a minimum, the agreement shall embody:

* * * * *

(8) The right of the sponsoring organization or the day care home to terminate the agreement for cause or, subject to stipulations by the State agency, convenience; and

* * * * *

8. § 226.20 is amended by removing the words "be served between other

meal types and" from paragraph (a)(3); by revising the paragraph heading of (d)(2); and by adding paragraph (o), to read as follows:

§ 226.20 **Requirements for meals.**

(a) * * *

(3) Supplemental food shall contain two of the following four components:

* * * * *

(d) *Additional food.* * * *

(2) *Lunch, supper or supplemental food.* * * *

* * * * *

(o) *Family-style meal service.* Meals may be served in a family-style setting.

(Sec. 2, Pub. L. 95-627, 92 Stat. 3603, 42 USC 1766 and Pub. L. 97-35)

Dated: February 19, 1985.

Robert E. Leard,

Administrator, Food and Nutrition Service.

[FR Doc. 85-5201 Filed 3-1-85; 8:45 am]

BILLING CODE 3410-30-M

Farmers Home Administration

7 CFR Parts 1807, 1822, 1902, 1930, 1944, 1951, 1955, and 1965

Predetermined Amortization Schedule System (PASS)

AGENCY: Farmers Home Administration, USDA.

ACTION: Final rule.

SUMMARY: The Farmers Home Administration (FmHA) implements a new regulation and related changes in other regulations governing loan payments and servicing in the new Automated Multiple Housing Accounting System (AMAS) which incorporates a Predetermined Amortization Schedule System (PASS) as the payment application method. The present daily interest accrual system (DIAS) for payment application applies subsidized loan payments as if they are amortized at the subsidized (interest credit) rate usually 1 percent. This creates an inequity because principal for subsidized loans is reduced faster than principal for nonsubsidized loans. This action is taken in response to general public requests for a payment application method and other loan servicing functions consistent with practices in the private sector and Office of Inspector General (OIG) audits suggesting change in FmHA payment application methods so subsidized and nonsubsidized loans are treated equitably. The effect of this regulation will be a change from DIAS to PASS as the method of applying loan payments for all new loans, transfers, reamortizations and voluntarily converted loans after the effective date of the regulation. The related changes allowed by an improved accounting system are better services to borrowers and more efficient money management by FmHA.

EFFECTIVE DATE: The effective date of this regulation will be May 1, 1985.

FOR FURTHER INFORMATION CONTACT: Jeanine L. Johnson, Senior Loan Specialist, Multiple Family Housing Servicing and Property Management (MHSPM) Division, Room 5321-S, Farmers Home Administration, 14th and Independence Avenue, SW., Washington, D.C. 20250, Telephone: (202) 382-9728.

SUPPLEMENTARY INFORMATION: This action has been reviewed under USDA procedures established in Departmental Regulation 1512-1 which implements Executive Order 12291, and has been determined "nonmajor." It will not result in an annual effect on the economy of $100 million or more; a major increase in costs or prices for consumers, individual industries, Federal, State, or local government agencies, or geographic regions; or significant adverse effects on competition, employment investment, productivity, innovation, or on the ability of United States based enterprises to compete with foreign-based enterprises in domestic or export markets.

This document has been reviewed according to 7 CFR, Part 1940, Subpart G, "Environmental Program." It is the determination of FmHA that the proposed action does not constitute a major Federal action significantly affecting the quality of human environment and according to the National Environmental Policy Act of 1969, Pub. L. 91-190, an Environmental Impact Statement is not required.

The FmHA programs and projects which are affected by this regulation are subject to intergovernmental consultation in the manner delineated in FmHA Instruction 1940-J, "Intergovernmental Review of Farmers Home Administration Programs and Activities," available in any FmHA Office.

CFDA numbers and titles: 10.405, Farm Labor Housing Loans and Grants; 10.415, Rural Rental Housing Loans; 10.411, Rural Housing Site Loans; and, 10.427 Rural Rental Assistance Payments.

FmHA implements a new Automated Multiple Housing Accounting System (AMAS) with borrower payments applied on PASS, to provide a loan accounting system consistent with the private sector and to provide incentive for borrowers to make timely loan payments. The design of AMAS incorporates recommendations in the President's Private Sector Survey on Cost Control (PPSSCC); requirements of Pub. L. 97-365 known as the Debt Collection Act of 1982; "Reform 88"; and Office of Management and Budget and Government Accounting Office requirements for government accounting system and automated data processing system design.

The benefits to the government from AMAS include better cash management, better control of subsidy funds, better data on use of loan and grant funds, improved account servicing to borrowers, more effective reports available to Congress and FmHA National, State and District Offices on funds and services provided to the public and equitable application of borrower payments whether subsidized or nonsubsidized.

Benefits to borrowers include easier understanding of FmHA's payment application method; ability to project payment applications to interest and principal; and ability to deduct rental assistance from payments made to FmHA.

This action incorporates new and improved administrative procedures made possible by the design of AMAS. The major changes are: Payments based on PASS; computer based use of funds and project data maintained by State and District Offices; computer based tracking of rental assistance; obligation and use of rental assistance maintained by fiscal year of obligation; payment notices for borrowers; better disclosure of payment application including application of subsidy; suspension of rental assistance in problem cases; and transfer of unused rental assistance between projects.

The proposed rule published April 18, 1984, included authority to suspend rental assistance in problem cases or credit sales and authority to reinstate to the present borrower, or a new borrower in the case of a credit sale, so the rental assistance is not lost to the project. Pub. L. 98-181 dated November 30, 1983, requires that, "the Secretary (of Agriculture) shall transfer rental assistance contract authority under this section (Section 521 of the Housing Act of 1949, as amended) from projects where such authority is unused after initial renting and not needed because of a lack of eligible tenants in the area to projects where such authority is needed." The originally proposed language of paragraph XV of Exhibit E of Subpart C of Part 1930 has been revised to incorporate this provision of Pub. L. 98-181.