
Agriculture in the WTO

The Current WTO Agricultural Negotiations: Options for Progress

Synthesis



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Preface

This document is a synthesis of a series of papers prepared for the International Agricultural Trade Research Consortium (IATRC). The papers were presented at a conference entitled “WTO Negotiations on Agriculture: Review of Progress” held in Washington D.C. on May 18, 2001. The co-organizers of the conference were Praveen Dixit, Economic Research Service (ERS) of the U.S. Department of Agriculture, and Tim Josling, Stanford University. The synthesis was prepared by Praveen Dixit, Tim Josling and David Blandford, Penn State University.

Four IATRC Task Forces were set up at the end of 2000, and each was asked to prepare a Commissioned Paper (CP) for the conference. Copies of the papers are available on the IATRC website. These papers and their authors are as follows:

Market Access: Issues and Options in the Agricultural Negotiations (CP 14)

Maury Bredahl, University of Missouri

Mary Burfisher, ERS/USDA

Karl Meilke, University of Guelph (Principal Author)

James Rude, University of Saskatchewan

Export Competition: Issues and Options in the Agricultural Negotiations (CP 15)

Philip Abbott, Purdue University

Susan Leetmaa, ERS/USDA

Linda Young, Montana State University (Principal Author)

Domestic Support: Issues and Options in the Agricultural Negotiations (CP 16)

Lars Brink, Agriculture and Agri-Food Canada

John Dyck, ERS/USDA

Lynn Kennedy, Louisiana State University (Principal Author)

Donald MacLaren, University of Melbourne

The Role of Product Attributes in the Agricultural Negotiations (CP17)

Julie Caswell, University of Massachusetts

David Orden, Virginia Polytechnic Institute

Tsunehiro Otsuki, World Bank

Donna Roberts, ERS/USDA (Principal Author)

Ian Sheldon, Ohio State University

Laurian Unnevehr, University of Illinois

John Wilson, World Bank

Two other papers were also given at the Conference, and are included in this synthesis:

Agriculture in the WTO: Background to Current Negotiations

Stefan Tangermann, University of Göttingen

Future Research Needs and Prospects and Role of the IATRC

Tim Josling, Stanford University and Praveen Dixit, ERS/USDA

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Executive Summary

The Uruguay Round (UR) of GATT negotiations instituted a new set of rules for agricultural trade, embodied in the Agreement on Agriculture (URAA) and its related commitments. It also resulted in a fresh attempt to regulate technical barriers to trade, primarily through the new Agreement on the Application of Sanitary and Phytosanitary (SPS) Measures and revision of the Technical Barriers to Trade (TBT) Agreement.

A key outcome of the URAA has been greater transparency. WTO Members imposed bound tariffs on their agricultural imports. The URAA established effective constraints on existing export subsidies and prohibited new ones. It established new rules that distinguished domestic policy instruments by their degree of trade distortion. However, country commitments were weak, and the effectiveness and workability of the URAA has been relatively untested in that area.

Many developing countries expressed the concern that they might have difficulties in importing adequate supplies of food under reasonable terms during the implementation of Uruguay Round reforms. These concerns were addressed in a ministerial decision (NFIDC Decision) that was adopted as a part of the UR Agreement.

The UR agreements disciplining product attribute measures have clearly reduced regulatory barriers to agricultural trade. However, the current multilateral rules have been challenged by events that were hardly anticipated in the last round.

Current status of agricultural trade policies

Duties on farm products remain very high, despite UR commitments to reduce agricultural tariffs. The global average of maximum permitted post-UR tariffs is 62 percent. By the end of 1999, 1371 Tariff Rate Quotas (TRQs), that allow certain quantities of imports at lower tariffs, had been notified to the WTO covering a wide variety of both bulk and processed products. Complex and variable tariffs are still used by a number of countries. The URAA allows countries to apply special safeguard (SSG) duties to counter import surges for products whose border protection was 'tariffed' and included in the country schedules.

Export subsidies are still widespread. Between 1995 and 1998, WTO members spent over US\$27 billion subsidizing exports. Global expenditures on export subsidies by WTO members have been greatest for dairy products – accounting for 34 percent of the total from 1995 to 1998. Officially supported export credits can also act as subsidies if the terms of loans are more favorable than those available privately. The use of export credits increased from \$5.5 billion in 1995 to \$7.9 billion in 1998.

The URAA established bindings on domestic agricultural support that were intended to constrain measures that increase domestic prices and distort trade by encouraging agricultural production or reducing consumption. Domestic support is highly concentrated in a few countries. The European Union, the United States and Japan account for 90 percent of total domestic support in the OECD countries. With a few exceptions, member countries have adjusted their domestic support policies to comply with the Agreement.

State Trading Enterprises (STEs) are prevalent in certain countries and markets. Over the last several years, notification requirements have been tightened; thirty countries have notified the WTO of the existence of nearly 100 state trading enterprises.

Since the conclusion of the UR, the adequacy of multilateral rules for measures that regulate product attributes (health and safety, quality and mode of production) has been called into question by new production technologies, disease outbreaks, and demands for greater domestic regulation.

The current negotiations

The current round of agricultural trade negotiations builds on the legacy of the Uruguay Round. Further reform of agricultural trading rules needs to be based on improved market access; additional constraints on export subsidies and equivalent practices; and clarification of the flexibility that countries have in granting domestic support so that it is minimally trade distorting. In addition, countries will need to clarify rules for food aid; the use of state trading enterprises in agricultural markets; special and differential treatment for developing countries; and rules for product attribute regulation.

Tariff cuts should be based on a formula that reduces high tariffs as well as lowering the average tariff towards that for non-farm products. TRQs should be expanded and their allocation made more transparent. Export subsidies should be eliminated by an agreed future date. In the meantime, rules should be considered for preventing circumvention. Export credit terms should be constrained by agreement, and the subsidy element involved in single-desk selling should be controlled. Domestic support should be further restrained, particularly that which is considered trade distorting, and the Peace Clause, if continued, should be restricted to Green Box measures.

Improved notification of food aid flows may be needed, but care should be taken that the volume of aid does not decline below the quantities needed. Clarification of the place of state trading agencies within the WTO should include consideration of competition in the markets concerned. The review of special and differential treatment could include the continuation of tariff preferences under specified conditions and clearer criteria to qualify for special and differential treatment.

The case for clarifying current WTO rules for product attribute regulations, rather than changing them, is strong. The causes of limited implementation of some aspects of the UR agreements need to be diagnosed before effective remedies can be prescribed. Further study of the economic effects of nascent measures, such as required labeling of production methods, should also be pursued before changes to the rules are considered.

The packaging of the outcomes in the agricultural negotiations has to reflect balance in at least four different dimensions. First and foremost, the outcome has to meet the major aspirations of both developed and developing countries. Second, the package has to reflect a balance between the interests of importing and exporting countries. Third, there has to be balance among commodities. Last, there is need for balance between agriculture and other areas. This final element would be easier to achieve if the agricultural talks were part of a comprehensive round of trade negotiations.

The Current WTO Agricultural Negotiations: Options for Progress*

I. Introduction

The Uruguay Round (UR) of GATT negotiations was a major step forward in international trade relations. Among its many innovations were a permanent trade body, the World Trade Organization (WTO), a strengthened dispute settlement mechanism, and agreements on intellectual property rights and services. The UR also instituted a new set of rules for agricultural trade, embodied in the Agreement on Agriculture (URAA) and its related body of commitments, and a fresh attempt to regulate technical barriers to trade in the agriculture and food sector, primarily through the new Agreement on the Application of Sanitary and Phytosanitary (SPS) Measures and revision of the Technical Barriers to Trade (TBT) Agreement. Considerable effort was devoted to designing new rules for agriculture, and at times it looked like the UR negotiations might break down due to the difficulty of achieving agreement. However, in the end, a framework for agricultural trade emerged which was very different from that which had existed before (see Box 1).

The implementation period for the UR agreements is now over, at least for the developed countries; a new round of negotiations on agriculture started in March 2000. The purpose of this report is to review the current state of the UR rules, assess the current situation in agricultural trade policy, and analyze options for further reform of agricultural trade.

II. What was achieved in the URAA?

A key effect of the Uruguay Round Agreement is greater transparency in agricultural policies. Notification requirements have created a large body of quantitative and qualitative information on agricultural policies in WTO Members. The WTO Secretariat has been summarizing this information and making it available to the general public. This has made the task of keeping up with the current negotiations easier for those who will be affected by the outcome.

A. Market Access

The primary test of the effectiveness of the new rules in the area of market access is whether countries have implemented bound tariffs, and whether these tariffs have remained within maximum agreed (bound) levels. This has generally been the case. With a few exceptions, WTO Members have imposed bound tariffs on their agricultural products. The major exception was removed when Japan replaced its quantitative import restriction on rice by a tariff in 1999, though Korea has yet to follow suit. A number of

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complaints¹ have alleged that importing countries have violated the requirement not to maintain, resort to, or revert to non-tariff measures (Article 4.2 of the URAA), where the justification has involved balance of payments problems. On the other hand, there are many cases, mainly in developing countries, where tariffs applied are below bound levels (Tangermann et al., 1997). Only a small number of complaints have been made to the WTO that a country has used an import regime in violation of its tariff binding.²

The nearly universal binding of agricultural tariffs has not, however, completely eliminated measures that resemble the non-tariff barriers that existed before the Uruguay Round. In some cases, countries have established sophisticated tariff regimes that act like non-tariff barriers. The EU's post-Uruguay Round entry price regime for fruit and

Box 1: Accomplishments of Uruguay Round Agreements

Agreement on Agriculture:

- converted non-tariff border measures to tariffs and bound all tariffs (i.e., cannot be increased without negotiation with other countries)
- reduced tariffs by 36 percent (on average) over six years from a 1986-88 base; and with a minimum reduction of 15 percent per tariff line (with a 24 percent reduction over ten years for developing countries)
- established rules for the application of additional (safeguard) duties (up to one-third of normal duties) if imports surge or if world prices fall below preset trigger price levels for goods subject to tariffication
- created minimum access commitments as a share of domestic consumption for products subject to tariffication
- reduced domestic support---as measured by the total Aggregate Measure of Support (AMS) from a 1986-88 base--- by 20 percent over six years. Domestic support considered minimally trade distorting (green box) not included. Direct payment for production-limiting program (blue box) not included in AMS reductions under certain conditions
- banned new export subsidies and introduced constraints on existing subsidies. Budget expenditures for export subsidies reduced by 36 percent, and volume by 21 percent, over the 6-year implementation period
- Developing countries subject to only two-thirds of the cuts in tariffs, domestic support, and export subsidies and over a period of 10 years

Other UR Agreements:

- New SPS Agreement established a framework to reduce trade-distorting aspects of animal, plant and human health measures
- Measures that stipulate production and processing methods are now disciplined by the revised TBT Agreement
- New TRIPS Agreement extended protection to geographical indicators for agricultural products, particularly wine and spirits
- GATT 1994 converted plurilateral agreements, such as the TBT Agreement, into multilateral agreements

¹ This account of complaints and disputes is based on the document "Overview of the State-of-play of WTO Disputes" on the WTO website as of 23 March 2001 (<http://www.wto.org>).

² See Tangermann (2000) for details of these complaints.

vegetables is similar to its former reference price system (Grethe and Tangermann, 1999). Variable tariffs used in Latin America have effects similar to variable levies (Tangermann et al., 1997). The EU's "maximum duty-paid import price" regime for cereals (also called a "margin of preference"), established at the request of the United States as a result of the Blair House II agreement, effectively continues the option to impose a variable levy (Tangermann et al., 1997). It is important, though, to note that all these policies are not legally inconsistent with tariff bindings agreed during the Uruguay Round, and that variable tariffs in Latin America and the EU, are below the bound tariffs.³

A controversial element of the URAA rules on market access is the Special Safeguard Provision (SSG) that protects goods subject to tariffication from surges in imports or depression in world prices. However, the SSG has not been used very much, and there has been only one dispute involving the provision.⁴ Equally controversial is the administration of the many tariff rate quotas (TRQs) in agriculture, under which countries specify import quantities that incur duties below the bound rates. Except for the banana case, which is of a very special nature, only three complaints have addressed that issue, but there is probably more dissatisfaction with TRQs than is apparent from formal WTO complaints.

B. Export Competition

Many observers consider the rules on export subsidies to be the most important element of the URAA, by establishing effective constraints on existing agricultural policies and the consequent effect on trading conditions. The implementation of the URAA rules on export competition should, therefore, be an important test for the reliability and effectiveness of the Agreement. Based on this criterion, the URAA appears to have worked rather well.

As far as the quantitative commitment on export subsidies is concerned, there has only been one case in which a country flagrantly exceeded its commitments on the volume of subsidized exports or budgetary outlays, and/or granted export subsidies on products not specified in its Schedule.⁵

³ In the early phase of the implementation of the URAA there was some discussion between the United States (and Canada) and the EU about the particular way the EU implemented its variable tariffs on cereals. However, the fundamental approach was not in question, only 'technical' aspects. The issue was settled when the EU adjusted its regime. More recently, Chile's price band regime was challenged in the WTO, but at the time of writing that case has not yet been settled, see Chile – Price Band System and Safeguard Measures relating to Certain Agricultural Products, complaint by Argentina (WT/DS207/1).

⁴ European Communities - Measures Affecting Importation of Certain Poultry Products, complaint by Brazil (WT/DS69).

⁵ The country concerned was Hungary, which claimed that it had erroneously overlooked some export subsidies that had actually been granted in the base period, and hence had wrongly specified commitments in its Schedule. The case resulted in long and heated debates in the Committee on Agriculture, and a complaint was brought before the WTO. In the end, Hungary was granted a waiver that allowed it to exceed its commitments on export subsidies by given margins, for an interim period ending in the year 2001. From 2002 on, Hungary will have to constrain its export subsidies to the levels originally bound in its Schedule.

For a while there was a debate in the Committee on Agriculture on whether the ‘credit’ provisions in Article 9.2(b) should allow countries to exceed their annual commitments on export subsidies if they had ‘underutilized’ them in previous years. This practice was finally accepted, and used in a number of cases (particularly by the EU).

It can be argued that many countries more than fulfilled their export subsidy commitments, by applying lower export subsidies than their commitments under the URAA, or by eliminating subsidies. Overall, WTO Members utilized less than 40 per cent of their allowable export subsidy outlays in the aggregate from 1995 to 1998 (see Table 1). It would be wrong to say that the ‘under-utilization’ of export subsidies by WTO Members was due to their efforts to make the URAA work even better than originally planned. There were many domestic agricultural policy developments that underlay this phenomenon, and high world market prices for some agricultural commodities during the URAA implementation period (in particular for cereals in 1995 and 1996) also helped. Moreover, ‘water’ was contained in the export subsidy commitments, since the base period chosen for setting the constraints was characterized by particularly large expenditures. However, based on the aggregate quantitative experience with the export subsidy commitments, this part of the URAA appears to have been successful.

Table 1: Export Subsidy Outlays: Commitments and Utilization

		1995	1996	1997	1998	1995-98
All WTO Members						
1 Commitments	mill. US \$	21,036	19,800	17,432	12,987	71,255
2 Notifications ^{a)}	mill. US \$	6,812	7,857	5,931	5,533	26,134
3 ‘Utilization’ [2/1]	percent	32.4%	39.7%	34.0%	42.6%	36.7%
European Union						
4 Commitments	mill. US \$	14,573	13,870	12,100	8,333	48,876
5 Notifications	mill. US \$	6,058	7,088	5,262	4,849	23,257
6 ‘Utilization’ [5/4]	percent	41.6%	51.1%	43.5%	58.2%	47.6%

^{a)} Subsidy outlays reported are not comprehensive for the years 1996 to 1998 as some countries had not yet notified their export subsidies by the time the WTO Secretariat produced its background paper.

Source: Calculated from figures in WTO (2000a).

It is also important to note that the mere existence of this new type of rule for agricultural trade policies, and the expectation that further reductions will be negotiated in the future round(s) of WTO negotiations, are important for the domestic agricultural policy debate in a number of countries. EU policies are, again, a prime example. Cuts in support prices agreed in 1999 were intended to make it possible for the EU to reduce, if not eliminate, export subsidies for some products. One of the major objectives of the ‘mid-term review’ of the CAP in 2002/2003 will be to reduce further the dependence of EU agricultural policies on export subsidies. In EU, and in other countries as well, the rules for agricultural export subsidies established under the URAA have proved effective, and this has improved the international market situation. Other countries also changed policies to meet export subsidy limits. Canada eliminated its rail subsidies for grains in 1995.

Switzerland began reforms in 1999 to eliminate state trading of dairy products. Australia replaced dairy export subsidies with rebates of a new production levy; it eliminated that levy in 2000.

Another important challenge to an agricultural trade policy under the WTO has had to do with Canada's dairy regime, which some countries felt was inconsistent with Canada's WTO obligations, in particular in the area of export subsidies.⁶ Though technically rather complex, the case essentially involves a producer-financed export subsidy.⁷ As this practice is not uncommon, the dispute has implications that go far beyond the Canadian dairy regime. The issue was whether the price discrimination regime in Canada amounted to an export subsidy as defined in Article 9 of the URAA, and hence whether Canada, which exported dairy products in excess of its export subsidy commitments, had violated its obligations. The panel found that Canada's regime amounted to a producer-financed export subsidy, and the Appellate Body agreed. Canada accepted the outcome, and embarked on a process of adjusting its policy. However, a WTO panel recently ruled that the steps taken were insufficient; this dispute may go on for some time.

The Canada dairy case, once it is finally settled, has the potential to contribute significantly to strengthening the export subsidy provisions of the URAA and their application. Canada has not denied the need to adjust its policy regime in response to the outcome of the case. It remains to be seen whether or how the more recently established regime will be adjusted again. In any case, the original ruling of the panel and the Appellate Body was rather firm, and the defendant country actually started to change its policy. One only needs to compare this outcome with ineffective disputes over GATT Article XVI:3 prior to the Uruguay Round to see how much the URAA has improved the situation for agricultural export subsidies.

C. Domestic Support

The URAA was most innovative in the area of domestic support by establishing new rules, which distinguish agriculture significantly from industry. Against this background it is somewhat ironic to find that this is the area where country commitments are the weakest, and where the effectiveness and workability of the URAA has been least tested. Since 1995, in many countries, levels of domestic support subject to reduction commitments, as measured by the current total AMS, have remained considerably below their commitments (see Table 2). In only two cases was the commitment level exceeded in individual years, and both were special.⁸ In all years since 1995 for which notifications are available, around one half of all WTO Members with domestic support notifications used less than 60 per cent of their domestic support commitments.

⁶ Canada - Measures Affecting the Importation of Milk and the Exportation of Dairy Products, complaint by the United States (WT/DS103/1), and Canada - Measures Affecting Dairy Products, complaint by New Zealand (WT/DS113/1).

⁷ The term 'producer-financed' is a euphemism, as it is domestic consumers who bear the cost, by paying higher prices.

⁸ In one case (Argentina, 1995), the point was made that the original Schedule had been established erroneously. In the other case (Iceland, 1998), 'excessive inflation' was given as a reason. See WTO (2000c) and the WTO documents mentioned there in these two cases.

To some extent, the significant slack that exists in many countries' domestic support commitments is due to the use of a generous base period. In the EU, and in the past for the United States, it also has to do with the creation of the blue box, which shelters a large part of actual support to farmers in the form of direct payments. In other cases, though, the low 'utilization' of domestic support commitments reflects policy changes, through which support has been decoupled from production and moved into the green box. The U.S. Federal Agricultural Improvement and Reform (FAIR) Act of 1996 is the most prominent example. Asian countries, especially Japan and Korea, also made considerable changes in agricultural policy in response to WTO commitments.

Table 2: Actual AMS Levels Relative to Commitments, 1995-99

Year	Current Total AMS as a percentage of Total AMS commitment levels (number of notifications)					Total number of notifications (out of 29 as of 1996)
	0-20%	21-40%	41-60%	61-80%	81% and over	
1995	7	2	4	8	6	27
1996	6	5	2	8	4	25
1997	5	5	1	5	6	22
1998	3	2	0	4	4	13

Source: Taken from WTO (2000c).

The fact that domestic support commitments have not (yet) proved restrictive may explain why there has only been one WTO complaint.⁹ That case contributed to reinforcing the methodology for calculating the AMS, and in that sense showed that the URAA is effective and operational in this area. Another part of the URAA rules on domestic support, though, still remains to be tested – the eligibility of policies for inclusion in the green box. There have been no legal challenges to the decisions made by countries to place their policy measures in the various boxes. Either the system is working rather well or the rules are deemed to have inadequate teeth to make a challenge worthwhile. If most countries are well within their allowable total AMS levels, it makes little sense to challenge Green Box policies to have them declared “Amber.”

To ensure that policies that qualify under the Green Box are not subject to challenge by rules that apply to non-agricultural subsidies, the URAA provided for “Due Restraint”. The Peace Clause, as this provision is known, specifies that domestic support measures that conform to the Green Box provisions are non-actionable and exempt from countervailing duties. Other domestic support is also immune to certain actions in some circumstances. The Peace Clause is scheduled to expire at the end of 2003.

Developing countries can exempt a somewhat larger set of policy instruments from commitment and reduction. It was recognized that government assistance for agricultural

⁹ Korea – Measures Affecting Imports of Fresh, Chilled, and Frozen Beef, complaint by the United States (WT/DS161/1), and the related case Korea – Measures Affecting Imports of Fresh, Chilled, and Frozen Beef, complaint by Australia (WT/DS169/1) examined by the same panel.

and rural development is an integral part of the development programs of developing countries. For such countries, investment subsidies for agriculture and input subsidies for low-income or resource-poor producers are exempt from reductions. Support to encourage diversification away from illicit narcotic crops is also exempt. These provisions are known collectively as Article 6.2 exemptions.

If the URAA is judged purely on the basis of the total level of support for agriculture, it appears to have had a limited impact. Domestic support levels in the European Union and the United States were as high in the late nineties as those in the 1986-88 base period. Support for the agricultural sectors of the main developed countries was at levels seen at the beginning of the Uruguay Round, although the year 2000 saw a modest decline in some countries (OECD, 2001a). There remain key sectors, such as dairy and sugar, where adjustments to less production/trade distorting outcomes have yet to take place. For these commodities, domestic producer/consumer prices are often high relative to international prices.

The URAA scores somewhat better in terms of the nature of domestic support. The Agreement has reinforced the shift from non-exempt (Amber Box) to exempt (Green Box or Blue Box) domestic support, even if it has not ensured that total support has been reduced. Countries have considerable flexibility under the provisions of the Green and Blue Box categories as well as under the *de minimis* provisions. An evaluation of the impact of the domestic support rules in the URAA must therefore rest on the effectiveness of this shift in reducing trade distortions.

D. Food Aid

The URAA and a ministerial decision address food aid. Article 10.4 of the URAA states that food aid (1) shall not be tied to commercial exports of agricultural products to recipient countries; (2) must be carried out in accordance with the FAO's "Principles of Surplus Disposal and Consultative Obligations," and (3) be provided fully in grant form or meet concessional terms, as provided in Article 4 of the 1986 Food Aid Convention. These rules incorporate the use of protocols and multilateral institutions that have developed over a long period of time.

Food aid was one of the concerns expressed by Least-Developed and Net Food-Importing countries, who anticipated difficulties in importing adequate supplies of food under reasonable terms during the implementation of Uruguay Round reforms. These concerns were addressed in a ministerial decision¹⁰ (NFIDC Decision) that was adopted as a part of the URA. The NFIDC Decision committed the WTO to:

- Review the level of food aid established by the Committee on Food Aid under the Food Aid Convention 1986 and to initiate negotiations in the appropriate forum to establish a level of food aid commitments sufficient to meet the legitimate needs of developing countries during the reform program;
- Adopt guidelines to ensure that an increasing percentage of basic foodstuffs is provided to least-developed and net-food importing developing countries fully in

¹⁰ Ministerial Decision on Measures Concerning the Possible Negative Effects of the Reform Programme on Least Developed and Net Food Importing Developing Countries.

grant form and/or on appropriate concessional terms in line with Article IV of the Food Aid Convention 1986;

- Give full consideration in the context of their aid programs to requests for the provision of technical and financial assistance to least-developed and net food-importing countries to improve their agricultural productivity and infrastructure.

One problem with the NFIDC Decision is the ambiguity of its language, making it difficult for the parties to agree whether or not commitments have been met. The WTO reviewed food aid levels and initiated negotiations under the Food Aid Convention (FAC). Food aid recipients consider the implementation of the FAC unsatisfactory, as donor commitments have declined. Eleven developing countries stated in their WTO position paper “Despite the promises, there has been no political will to activate the Marrakesh Decision in order to address the problems of net-food-importing developing countries (NFIDC). This had been the avenue developing countries had expected to receive compensation for the negative effects of liberalization” (WTO 2000b). This failure is one reason for reluctance on the part of many developing countries to negotiate further reforms (Bridges Weekly Trade Digest 2000a; Bridges Weekly Trade Digest 2000b; WTO 2001).

E. Product Attribute Issues

During the Uruguay Round, countries negotiated new and revised agreements both to increase the scope and the specificity of disciplines on safety and quality regulations. A new SPS Agreement sets out more explicit rules for the regulation of safety attributes; the revised TBT Agreement now disciplines measures that regulate production and processing methods; and the new TRIPS Agreement extends intellectual property protection to geographical indicators (GIs), which are often used to differentiate agricultural products in the marketplace.

The SPS Agreement introduced the most sweeping changes to previous rules. The Agreement reiterates earlier commitments under the GATT to apply technical restrictions only to the extent necessary and to avoid unjustifiable discrimination among members, but also requires regulators to: 1) base measures on a scientific risk assessment (science-based risk management); 2) recognize that different measures can achieve equivalent safety outcomes (equivalence); 3) allow imports from regions that are free or nearly free of pests or diseases (regionalization); and 4) provide notification through the WTO of proposed regulations that affect trade (transparency). Adoption of international standards (harmonization) is encouraged, but not required. Dispute settlement is available when WTO countries are unable to resolve differences through bilateral negotiations.

Several cases brought before the WTO related to product attribute regulations have dealt with SPS measures, and provided tests of the application and interpretation of the SPS Agreement (Roberts, 1998). Three of these cases reached the Appellate Body: the EU’s ban on hormone-treated beef, Australia’s ban on salmon imports, and Japan’s testing requirements for new varieties of fruit. The most prominent of these was the hormones

case against the EU.¹¹ That case showed the “success” of the SPS disciplines, in the sense that the agreement had all the elements necessary to reach a finding on the measure concerned; it was also successful in the sense that both the panel and the Appellate Body could reach reasonably clear conclusions that the EU had violated its obligations under the agreement. However, the case was less than successful in achieving changes in the measure found to be inconsistent with the agreement: the EU has not changed its policy to make it conform to the WTO ruling. One might argue that even that apparent failure was not total, since the EU has in principle accepted the verdict, tolerates the sanctions imposed on its exports, and is trying to negotiate compensation. The success of the Agreement has been less ambiguous in the other two cases: both Australia and Japan agreed to revise their measures when they were found to be in violation of the SPS provisions.

Beyond the disputes, there is evidence that the SPS Agreement has improved transparency, encouraged greater use of risk assessment as a basis for regulation, and encouraged animal disease control measures in delineated regions (Roberts, Josling and Orden , 1999). There has been less progress in the areas of equivalence and harmonization. The assessment of measures to determine whether they produce equivalent risk outcomes is generally both time and resource-intensive because production practices and the incidence of risks vary widely across countries, and countries have been reluctant to allocate additional resources to verify claims that would increase imports. The impact of harmonization on trade appears to be constrained both by the insufficient number and infrequent adoption of international standards. The character of international standards as a public good leads to an expectation of under-investment in their creation, leading not only to too few international standards, but also to too many outmoded standards.

The impact of the TBT Agreement on the regulation of other quality attributes of agricultural products is more difficult to ascertain: no dispute panel reports (related to food or any other products) have been decided on the basis of this agreement. However, the “mutually agreed solutions” to formal complaints that have been notified to the WTO, such as those against the EU’s labeling regime for different species of scallops, indicate that the definition of like products and the assessment of whether measures are least trade restrictive are likely to be of key importance.

The application of the TRIPS Agreement to agricultural products appears to be proceeding smoothly. The sole TRIPS complaint related to an agricultural product has been made by the United States which claims that the EU’s trade regime for protecting the GI “Budvar” undermines legal protection for pre-existing trademarks.

¹¹ European Communities – Measures Affecting Meat and Meat Products (Hormones), complaint by the United States (WT/DS26), and Canada (WT/DS48).

III. Current Situation in Agricultural Trade Policy

A. Market Access Conditions

1. Border Measures in Agriculture

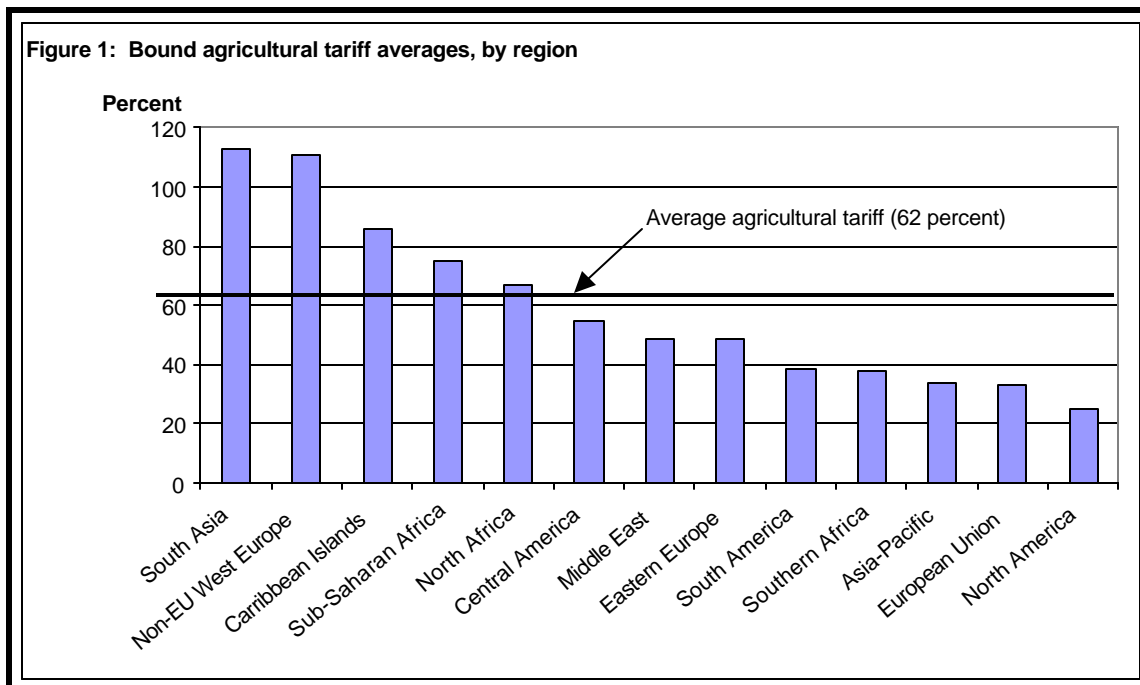
Despite the commitments made in the Uruguay Round to reduce agricultural tariffs, duties on farm products remain very high. Gibson *et al.* provide a comprehensive, comparative analysis of post-UR tariff rates by country and commodity.¹² They estimate the global average of post-UR bound agricultural tariffs at 62 percent.¹³

Regional average tariffs for WTO members range from an *ad valorem* tariff equivalent of 25 percent to 113 percent (Figure 1). With the exception of the high tariff region of non-EU Western Europe (104 percent), the groups with the highest tariffs are composed of developing counties: Africa, the Caribbean and South Asia have average bound tariffs ranging from 71 to 113 percent -- all above the global average of 62 percent. Representative OECD countries with agricultural tariffs below the global average include: Canada (24 percent), the EU (30 percent), Japan (33 percent), Mexico (43 percent) and the United States (12 percent).

Gibson et al. aggregated agricultural commodities into 46 groups and found that average bound tariffs varied from 50 to 94 percent. The average tariff for eighteen of the groups, including tobacco, dairy, meats, sugar, sweeteners, and several categories of vegetables, grains, grain products, and breeding animals exceeded the average for all products (Figure 2). Tariffs on the remaining 28 commodity groups fell below the 62 percent average tariff. Even the commodity groups with the lowest bound tariffs (i.e., coffee, fiber, several fruit categories, spices and live horticulture) have a high degree of potential protection with an average permitted tariff of 50 percent. OECD bound tariffs are very high in many sectors including dairy (116 percent), grains (78 percent), livestock (82 percent), and sugar and sweeteners (64 percent). These are the sectors in which some OECD countries use megatariffs (defined as tariffs over 100 percent), and in which the number of notified TRQs is concentrated. OECD tariffs are relatively low in other sectors. Because tariff spikes for sensitive commodities characterize OECD tariff profiles, there is a large dispersion, or variation, in tariffs across commodities.

¹² The analysis is based on tariff data from several sources, in particular the Agricultural Market Access Database (AMAD), a database of post-Uruguay Round bound tariffs, tariff rate quotas, and some applied tariffs for about 40 WTO members (available at www.AMAD.org). Other tariff data are from the WTO Secretariat and UNCTAD.

¹³ This simple (unweighted) average of post-UR bound agricultural tariffs includes the *ad valorem* equivalents of specific tariffs which are in some cases very high, and whose values depend on prices. It also includes the over-quota tariff in TRQ regimes.

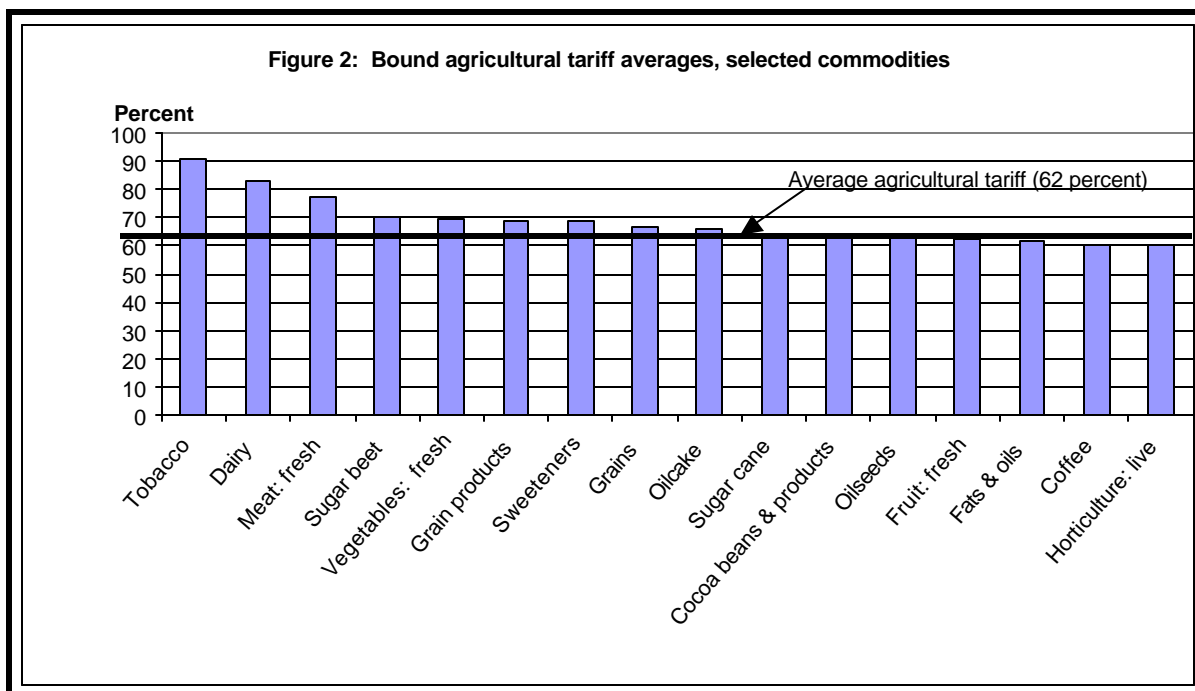


Source: Gibson, Wainio, Whitley and Bohman. 2001.

Non-OECD countries tend to have higher average bound tariffs than OECD countries, but with less variation across commodity groups. They have high tariffs for the same commodities as OECD countries, except that tobacco, rather than dairy, has the highest average tariff. Non-OECD countries use megatariffs (over 100 percent) more than OECD countries. Many of the megatariffs were not subject to reduction under the URAA because they were established as ceiling bindings.

It is important to note that some of the tariffs actually applied are considerably lower than the bound rates in the WTO schedules, particularly in developing countries. For example, the 1998 applied rate for Latin American countries of 13 percent is less than one-third of the average bound rate of 45 percent.

Although TRQs were designed to increase market access for commodities that previously faced quantitative barriers, high in-quota and over-quota tariffs show that TRQs can impede trade significantly. Across all WTO members, the average over-quota tariff is 123 percent. Five countries have average over-quota tariffs of at least 150 percent. In certain instances, the over-quota tariffs exceed 1,000 percent (e.g., the Japanese tariff on dried peas). Across WTO members, the simple average in-quota tariff is 63 percent – close to the average for all types of tariffs of 62 percent. In general, in-quota tariffs are less than 50 percent, but a few very high tariffs raise the simple average. TRQ regimes may have provided less market access than the architects of the URAA wished.



Source: Gibson, Wainio, Whitley and Bohman. 2001.

2. Tariff Dispersion Across Countries

Tariff dispersion raises two issues. First, non-uniform tariffs introduce relative price distortions that can worsen resource misallocation. Second, there is concern, especially among developing countries, that tariff dispersion often takes the form of tariff escalation – low rates on intermediate inputs (such as bulk farm products) and high rates on final products (i.e., processed foods). This results in high effective rates of protection (ERP) for value added products.¹⁴ Wainio et al. (2001) find that in both the U.S. and the EU, tariffs have a U-shaped distribution over commodity categories that are classified by level of processing. Bulk commodities have higher rates of protection than intermediate products, with tariffs being the highest on consumer ready items.¹⁵ Japanese tariffs are highest on bulk products. Canada appears to have tariff escalation. However, comparing tariffs across broad commodity groups is only a rough indicator of escalation since it does not capture input-output relationships among commodities. More research on a commodity-specific basis is needed before we can be more definitive on the extent of tariff escalation.

2. Tariff Rate Quotas

At the end of 1999, 1,371 TRQs had been notified to the WTO covering a wide variety of both bulk and processed products. Although TRQs cover only six percent of tariff lines, they are prevalent in sensitive sectors such as meat, dairy, sugar and cereals. Only 37 of

¹⁴ Value added refers to the contribution of primary factors (labor, capital and land) to a sector's output, and can be roughly calculated by subtracting the costs of intermediate inputs from the value of production.

¹⁵ The category of consumer ready items includes some unprocessed products such as apples and bananas.

the 137 WTO members use TRQs. Abbott and Morse (2000) examined tariff-quotas for 14 developing countries and found only a few cases of binding quotas. Rather, the TRQ was applied as a simple tariff (i.e., no over-quota tariff or effective quota). Eastern European countries also appear to be using TRQs frequently as simple tariffs. That group of countries only enforces 65 percent of their TRQs. A non-applied TRQ would allow those countries to raise their tariffs if they were to join the EU. Norway and Iceland account for 322 TRQs, but 90 percent of those are administered as simple tariffs. In fact, quota restrictions are applied for only 50 percent of the TRQs notified to the WTO. As a result, enforced TRQs are concentrated in a relatively small number of developed countries that use them to protect sensitive products.

The WTO identifies seven different methods of administering TRQ access: applied tariffs, first-come first-served, licenses on demand, auctioning, historical allocation, state trading importers, and producer groups. Applied tariff administration, allowing unlimited imports at the in-quota tariff, accounted for 47 percent of TRQs in 1999. Since this method is equivalent to a pure tariff, it has the corresponding benefits of predictability, transparency, non-discrimination, and efficient transmission of market signals. An applied tariff method is the least distorting because it does not create economic rents, inducing high-cost exporters to enter the market, and the level of fill is determined by import demand. The remaining methods of administration are all less desirable, but each has strengths and weakness as an allocation device.

A first-come first-served method allows the earliest imports to enter at the in-quota tariff rate up to the quota level. In 1999, 11 percent of TRQs were administered using this method. License on demand is a modified version of first-come first-served – if demand for import licenses exceeds the quota, the amount allocated to each applicant is reduced proportionately. This is the most popular administration method, after applied tariffs, with 25 percent of the TRQs allocated in this manner. Neither first-come first-served nor license on demand distinguishes between high and low-cost exports, and the existence of rents may attract inefficient supplies. Historical allocation accounted for five percent of TRQ administration methods in 1999. Although market conditions change, this method perpetuates past patterns of trade, thereby increasing the risk of under-fill and a biased distribution of trade. This method will not ensure that low-cost suppliers provide the imports.

Assigning quota rights to state trading enterprises or domestic producer groups is potentially the most distorting method of administering quota; it has not been a frequent choice. In 1999, STEs administered two percent of the TRQs; producer groups administered one percent. Both state traders and producer groups have filled their quotas. The simple average fill rates under state trading, for the period 1995-98 was 92 percent – the highest fill rate of all methods. However, these high fill rates may not reflect improved market access, as the trade flows already existed prior to the URAA. While quota fill, for existing access, is generally not a problem, the inefficient distribution of trade is. Additional market access may not produce such high fill rates and the decision to import may not be based entirely on commercial considerations. Imports controlled by producer groups can also minimize competition and may adversely affect the quality of imports.

Economists propose auctions as the most efficient method to allocate quotas.¹⁶ An auction distributes economic rents and prevents high-cost imports from filling the quota. In 1999, only four percent of TRQs were administered by auction and fill rates were low (under 40 percent in 1995 and 1996). If the transactions costs of participating in an auction are high, the tendency for underfill will also be high.

3. Variable Duties

When a bound tariff is significantly above the rate at which tariffs are typically applied, an importing country retains discretion with respect to the level of protection. Sometimes this discretionary power is formalized in instruments such as Latin American “price bands” and the EU “margin of preference” for grains. Price bands act as variable-rate surcharges, effectively setting a floor on the import price so that applied tariffs can be adjusted in response to variations in international prices. Chile, the Andean Pact, and Honduras employ price band regimes.

Under the URAA, the EU agreed to maintain a “margin of preference” for grains, so that imports of wheat, barley, rye, corn, and sorghum are subject to tariffs that maintain the duty-paid import price at 155 percent of the EU intervention price. After the implementation of Agenda 2000, the maximum duty-paid import price will be 157 euros per tonne.¹⁷ Given that the EU Commission adjusts its grain import tariffs every 2 weeks in response to changes in U.S. market prices, the mechanism works almost identically to a variable levy (Morath 1997).¹⁸ By controlling the duty paid import price, the EU can largely insulate its domestic market from world price fluctuations.

4. Safeguards

The URAA allows countries to apply special safeguard (SSG) duties to counter import surges for products whose border protection was ‘tariffed’ and included in the country schedules. Rules governing SSGs differ from those governing general safeguards in two important respects: actions are exempt from the obligation to compensate, and from the threat of suspension of equivalent concessions or other obligations (Perkins 1996); and SSGs may only be invoked during the reform process as detailed in the preamble to the URAA. However, if the reform process extends beyond the initial six-year period envisioned in the URAA, the SSG would be available during that extended period.

The SSG provisions allow the imposition of an additional tariff when certain criteria are met – either a specified rapid surge in imports (volume trigger), or, on a shipment-by-shipment basis, a fall of the import price below a specified reference price (price trigger). For the volume trigger, higher duties only apply until the end of the year in question. For the price trigger, an additional duty can only be imposed on the shipment concerned. Additional duties cannot be applied to imports within tariff rate quotas.

¹⁶ If quota rights could be traded in secondary markets many of the inefficiencies of quotas would disappear and the allocation method would be less important.

¹⁷ The value of 157 euros per tonne is 155 percent of the intervention price of 101 euros per tonne.

¹⁸ Where the binding does occur is in the relationship between the duty paid import price and the internal price. The fact that grains are now subject to a maximum rather a minimum import price is an improvement over the pre-URAA variable levy system.

Of the 137 WTO members that notified TRQs, only 38 reserved the right to use SSGs in their URAA schedule of commitments. The percentage of agricultural tariff lines covered by SSGs ranges from less than one percent for many developing countries to 9 percent for the United States, 12 percent for Japan, 31 percent for the European Union, 49 percent for Norway, 59 percent for Switzerland and 66 percent for Poland. The number of tariff items that could potentially be protected by SSGs ranges from 10 for Australia to 961 for Switzerland. The coverage across product categories reflects the degree of sensitivity to liberalization in each country. Product coverage is concentrated in dairy for the United States; cereals for Japan; and meat, dairy products, fruits, and vegetables for the European Union. The United States declared coffee and tea to be covered by SSGs to prevent the entry of sugar in dry or powdered beverage preparations. Switzerland and Norway reserve the right to use SSGs across almost all products.

Despite the broad coverage across products, few SSG actions have been taken. Since 1995, only the European Union, Japan and the United States have notified SSG actions in almost all years. Of 436 price-based actions reported over the five-year period, the United States accounted for over one-half, Poland for one-third and the European Union for about a tenth. Price-based actions tended to be directed at relatively small volumes of imports from specific sources. Of 213 volume-based actions, the European Union and Japan combined accounted for over 90 percent, with the EU alone accounting for almost 60 percent. The European Union used the volume-based SSG for fruits (particularly citrus), and vegetables (particularly tomatoes).

In practice, the SSG provision appears to have been used to balance internal markets by the United States, the European Union and Japan. In the case of the United States, the application of price-triggered SSG duties on relatively small quantities of individual dairy product imports, signaled to exporters that their products would face routinely applied SSG duties when trying to gain access to the U.S. market. The European Union used the SSG, in concert with other policies and regional agreements, to balance internal markets for perishable fruits and vegetables by restricting imports.

Overall, the special safeguard provisions of the URAA have not been a haven for countries seeking to prevent surges in imports. However, for a period after the implementation of the URAA, international and national prices for many agricultural products were high by historical standards and so would not have triggered efforts to limit imports. Only Poland seems to have resorted to SSGs on several occasions to counteract inflows of products. The United States has used the price-trigger to place duties on dairy products, peanuts and sugar-containing powder and dry beverages.

B. Export Competition Conditions

1. Export Subsidies

Between 1995 and 1998, WTO members spent over US\$27 billion subsidizing exports. The EU accounts for nearly 90 percent of the expenditures, Switzerland for 5 percent, and the U.S. for less than 2 percent (Table 3). The EU is the largest user of export subsidies in both value and volume terms. According to WTO notifications, the EU spent an average of \$6 billion annually from 1995 to 1998 on export subsidies. Over the same period, the EU's volume of subsidized exports averaged about 28 million tons annually plus 3.6

million hectoliters (95 million gallons) of wine and alcohol. From 1995 to 1998 the EU subsidized nearly all of its exports of coarse grains, butter and butter oil, beef, and skim milk powder. The majority of wheat and other dairy exports also required subsidies. Switzerland subsidizes exports of breeding cattle and horses, dairy products, fruit, potatoes, and processed products. Dairy products account for 65 percent of Swiss subsidy expenditures and nearly 80 percent of subsidized export volume – averaging nearly US\$230 million and 59,000 tons per year. Processed products account for 29 percent of expenditures for over US\$102 million per year, on average (volumes are not notified). Nearly 98 percent of U.S. export subsidy expenditures have been for dairy products (under the Dairy Export Incentive Program), just under two percent for poultry, and less than one percent for coarse grains (which were subsidized in 1997 under the EEP).

Table 3. Expenditures on Export Subsidies, 1995–1998, \$U.S million.

	Expenditures	Percent of total
European Union	24,369	89.4
Switzerland	1,403	5.1
United States	406	1.5
Norway	341	1.3
Rest of World	728	2.7

Source: WTO Notifications

The EU and Switzerland rely on export subsidies more than most WTO members because they support producers through high internal prices, which stimulate production above domestic needs and commercial export possibilities. Both also employ import barriers to keep cheaper imported products out of their domestic markets. The size of export subsidies change with world price and exchange rate fluctuations, as the price gap between the domestic and world price is the per unit export subsidy.

Global expenditures on export subsidies by WTO members have been greatest for dairy products – accounting for 34 percent of all export subsidy expenditures from 1995 to 1998. Beef is the single commodity with the largest subsidy expenditures – 21 percent of subsidies, averaging \$1.4 billion/year. Grains, sugar (\$745 million/year) and incorporated products (processed products) together accounted for 35 percent of expenditures.

Most countries report that their export subsidies have been below permitted maxima. During the URAA implementation period, the percentage of both volume and value commitments that were filled increased, as permitted levels of subsidization decreased and world prices fell. Based on WTO notifications from 1995 to 1998, members came closer to filling volume commitments than to expenditure commitments for most commodities, even though WTO members agreed to larger cuts in their expenditures. Although past WTO notifications have shown that the value limit has been less restrictive than the volume limit, this could change if world prices remain low.

The URAA does not place explicit restrictions on per unit subsidies; consequently the size of subsidies has varied greatly across countries and commodities. Subsidy expenditures on a dollar per ton basis have been largest for such high-value products as

alcohol, wine, and fresh flowers. However, those commodities account for less than 1 percent of subsidized export expenditures and volume. In terms of sectors, dairy has had the largest subsidies per ton. One would expect such subsidies to have decreased over the implementation period of the URAA, because both permissible volume and value limits were declining. The use of the rollover provision mitigated that decline and in some cases subsidies increased. Generally, export subsidies trended downward, but it is unclear whether this was due to market conditions and exchange rates, or to real reductions in the difference between domestic and world prices.

2. Export Credits

Short-term export credit is important to many international transactions. Governments are commonly involved in export credit activity, both for agriculture and for other commodities. The OECD and the WTO refer to this government involvement as “officially supported export credit”. Government involvement can include:

- Public and parastatal agencies (including state traders) that offer credit;
- Interest rate subsidies offered by government;
- Government assumption of default risk for private loans; and
- Publicly supported or subsidized insurance offered to private lenders.

Default risk guarantees are the most common form of officially supported export credit for agricultural commodities. Insurance schemes and credit offered by state trading agencies are also used. Explicit interest rate subsidies are uncommon.

Officially supported export credits are a subject for WTO negotiations because “Government supported export credits are seen as a way of circumventing export subsidy commitments because interest rates and repayment terms can be easier than under normal commercial conditions” (WTO 2001). Disciplines on officially supported export credits are likely to be considered in future negotiations on export subsidies; the European Union proposes that export credits and other forms of export subsidies be disciplined.

Officially supported export credits can act as subsidies if the terms of loans are more favorable than those that would have been available privately. For example, a subsidy element would be present if the interest rate charged does not reflect fully country risk premiums. The extent of the subsidy depends on interest rates relative to market rates (appropriately reflecting risk), fees charged, down payments required, and term of the loan. The longer the term for a given interest rate, down payment, and fee structure, the greater the subsidy element. Since risk premiums reflect default risk (at least in theory), the subsidy element of programs that involve default risk guarantees can be gauged from the extent to which government budgetary outlays are required to pay off guarantees.

A recent study by the OECD, based on a survey, provides the most up-to-date information on the extent and nature of officially supported export credit programs. That report indicates that the use of export credits increased from \$5.5 billion in 1995 to \$7.9 billion in 1998. Credits represented 3.6 percent of the value of total agricultural exports in 1995 and 5.2 percent in 1998. The expansion in use of officially supported export credits was likely due to deteriorating financial market conditions, especially the Asian financial crisis in 1997. The OECD report shows substantially different interest rates, and hence

subsidy values for the beginning of 1998 versus the end of 1998, reflecting the continuing financial crisis.

The OECD's estimate of the subsidy value of export credit programs in 1998 averaged 3.6 percent of total export value. There were only four countries for which subsidies exceeded one percent: 6.6 percent in the U.S., 3.8 percent in Norway, 3.8 percent in France, and 1.2 percent in Canada. Given these relatively small subsidies, distortions in trade patterns due to export credits are likely to be relatively small.

Less than half of the loans offered under officially supported export credit programs are for a term of more than one year. More than 96 percent of the loans for greater than one year are from the United States. As a consequence, most of the subsidy value estimated for these programs is through U.S. programs (88 percent). The European Union accounts for seven percent of export credit subsidies, Canada accounts for 4 percent, and Australia for one percent. Thus, the potential use of export credits as subsidies is largely a U.S. issue. It should be noted, however, that since the 1995 Uruguay Round Agreement the United States has relied largely on export credits rather than direct export subsidies (such as EEP), whereas the European Union has relied on direct export subsidies.

Bulk cereals are the most important commodity group subsidized. More than one-third of subsidies in 1996-97 went to cereals, and up to 14.5 percent (in 1997) of cereal exports received credit subsidies. However, officially supported export credit programs exist for a wide variety of commodities. The OECD also notes that most subsidized credits are applied to trade between its member countries. The least developed countries received only 0.2 percent of export credits, and food-importing developing countries received only 8.9 percent of credits. The OECD concludes that disciplines on agricultural export credits would not harm poorer food importing countries greatly, because historically they have not been major beneficiaries of the programs. The OECD suggests that this is indirect evidence that liquidity constraints for such countries are not being relieved, and the concerns raised in the Uruguay Round Agreement Ministerial Decision are moot. However, the same study shows increasing use of export credits during the Asian financial crisis, when liquidity constraints were likely to have been binding.

3. Export Taxes

The URAA did not discipline export taxes. Export taxes had not been used by major exporters for many years, and it is likely that negotiators believed they would not be used in the future. However, in 1995-96, world wheat and barley prices rose above the EU support price for grains. EU exports were drawing down domestic stocks; the EU instituted export taxes to prevent domestic prices from rising further and disadvantaging domestic end-users such as livestock feeders and millers. The taxes reduced EU exports. This was the first time that the EU had taxed grain exports since 1974. Since the EU is a large player in world grain markets, reductions in its exports in a time of scarcity resulted in a larger global price increase than would otherwise have occurred.

The Czech Republic, Hungary and Poland also employed export taxes on grains during the URAA implementation period. While support for restrictions on export taxes is widespread, developing countries, in particular, support disciplines on export taxes to prevent countries from forcing the burden of adjustment onto world markets. An

argument could also be made that discipline on export taxes would limit the exercise of market power in trade, but that has not been an important element in the debate.

Developing countries also employ export taxes. The use of export taxes on primary products is, for many of the poorest developing countries, a major means of generating tax revenue. Egypt used to maintain domestic cotton prices below the world price, taxing its producers, and until 1994 Argentina taxed exports of wheat, sometimes at levels of 25 percent or more.

C. Domestic Support Conditions

The URAA established bindings in the area of domestic agricultural support mainly through limits on the Total Aggregate Measurement of Support (AMS). Reduction commitments were intended to constrain domestic support measures that encourage agricultural production or raise consumer prices and are therefore considered to distort trade (Amber Box policies).

The URAA also specifies measures not subject to reduction. In addition to the *de minimis* provisions, countries are not required to include direct payments under certain production-limiting programs (Blue Box policies) in their total AMS. More widely applicable are the exemptions for Green Box policies that are considered to have no, or at most minimal trade-distorting effects or effects on production. The Peace Clause specifies that domestic support measures that fully conform to Green Box provisions are non-actionable and exempt from a variety of actions (e.g., from the imposition of countervailing duties). In addition, developing countries can exempt a somewhat larger set of policy instruments from reductions.

1. Amber Box

In meeting Total AMS commitment levels agreed in the URAA, members of the WTO were required to provide notification of agricultural support to the WTO Committee on Agriculture. Domestic support is highly concentrated in a few countries: the European Union, the United States and Japan account for 90 percent of total domestic support in the OECD countries (OECD, 2001b). With a few exceptions, member countries have adjusted their domestic support policies in order to comply with the Agreement. Of the Cairns Group countries, only South Africa (97 percent) and Thailand (79 percent) were close to the limit on support in 1997; Australia was at 25 percent, while Costa Rica and New Zealand were apparently providing no support at all through Amber Box policies.¹⁹ The corresponding figure for the European Union (average of 1995 - 1998) was 66 percent, for Japan (average of 1995 - 1998) it was roughly 59 percent, and for the United States (average of 1995 - 1997) it was 27 percent.

One way in which countries have been able to reduce their AMS levels to meet their URAA commitments is by shifting domestic support from non-exempt to exempt categories. Over 60 percent of the domestic support in OECD countries is now excluded

¹⁹ The Cairns Group consists of Argentina, Australia, Bolivia, Brazil, Canada, Chile, Colombia, Costa Rica, Fiji, Guatemala, Indonesia, Malaysia, New Zealand, Paraguay, Philippines, South Africa, Thailand and Uruguay.

from reduction commitments (OECD, 2001b). The structure of support ranges from New Zealand with all of its support in the Green Box category to the European Union with less than 25 percent of its support in that category.

2. Blue Box

The EU used the Blue Box for its compensatory payments under the 1992 reform of the Common Agricultural Policy (CAP); the U.S. used the Blue Box for its 1995 deficiency payments. Japan placed its rice policies in the Blue Box in 1998, replacing the rice support formerly subject to reduction in the Amber Box. Other countries utilizing this provision include Norway and, in the past, Iceland and the Slovak Republic. In 1995, \$35 billion of blue box support was notified to the WTO, of which 77 percent was in the EU. With the elimination of US deficiency payments, the total dropped to roughly \$27 billion in 1996 – 96 percent of which was in the EU.

3. Green Box

The use of green box measures expanded during the implementation period for the URAA. According to the WTO, several countries, including Australia, Canada, Korea and the United States, notified new or modified green box measures. A total of 63 new green box measures were notified for 1995-98. In 1996, \$127 billion of green box support was notified to the WTO. The two leading categories of support were domestic food aid (32 percent) and infrastructural and general services (28 percent). Other forms of support, such as investment aids, environmental programs and decoupled direct payments each accounted for 6-8 percent of total green box support.

D. Food Aid Conditions

Food aid is used to alleviate hunger due to natural disaster or political unrest. It is also used in development projects such as food-for-work, school feeding, and health and nutrition programs. Food aid programs began in the 1950s, due to the simultaneous existence of agricultural surpluses in the United States and Canada and both sporadic and systemic food shortages in developing countries. Since the 1950s other countries have become important food aid donors, and donors differ in the importance of humanitarian, producer support and political objectives in their food aid programs (Ruttan 1996; Barrett 1999; Christensen 1999). Particularly in the United States, food aid has been used as a mechanism to dispose of public stocks and as a tool for market development.

A mix of national and multilateral agencies provides food aid. The United States continues to be the largest donor – in the 1990s it provided 40 to 60 percent of total donations. Multilateral agencies have delivered 28 to 42 percent of food aid since 1994. Most multilateral aid is delivered through the United Nations World Food Program. Cereal food aid averaged less than 0.5 percent of world cereal production, or around 9 percent of cereal imports by low-income food deficit countries. Actual deliveries exhibit substantial variability. Food aid was nearly 13 million metric tons (mmt) in 1994, declined to 7.2 mmt in 1996, and rose to 14.5 mmt in 1999. While a variety of foods are used as aid, cereals continue to account for around 87 percent of the total (WFP 2000).

For recipients, the role of surplus disposal in donor food aid programs has resulted in less food aid during times of global shortages, when prices are high and stocks are low. The delivery of aid has been, and to some extent continues to be, greatly influenced by availability. The first food aid convention was negotiated in 1967 in an attempt to address recipient needs better. The Food Aid Convention (FAC) is a forum in which donors commit to provide a minimum amount of aid for a specified period of time. The 1967 convention guaranteed minimum commitments of 4.5 mmt of food aid. This rose to 7.5 mmt in 1986, although actual donations exceeded the minimum in many years. In 1999, donors to the FAC decreased their pledged commitment to 4.8 mmt – the lowest amount since the initiation of the program. It should be borne in mind that actual donations were nearly three times the commitment due to substantial surpluses. Current donor obligations under the FAC are expressed in terms of tons of food, not dollars, which should assist the maintenance of minimum aid levels regardless of cereal prices. However, in recent years the United States has continued its historical pattern of varying food aid donations in line with its wheat and other cereal stocks.

Another factor impinging on the adequacy of food aid is that emergency aid more than doubled between 1990 and 1999 – rising from 19 to 43 percent of total donations. The increase in complex and long lasting emergencies means that smaller amounts of food aid are available to support development objectives.

Several developing countries have expressed concerns that the Uruguay Round NFIDC decision has not been adequately implemented. In December 2000, the General Council of the WTO instructed the Committee on Agriculture to examine problems facing food importing developing countries in this context. This committee has identified three issues in discussion over implementation: a food financing facility and technical and financial assistance for improving agricultural productivity and infrastructure.

E. State Trading Conditions

The treatment of State Trading Enterprises (STEs) is the subject of on-going discussion in the WTO. State trading comes under the purview of the UR Understanding on Interpretation of Article XVII, which established a working definition of an STE and notification requirements, as well as the URAA, which ensures that such enterprises are subject to rules on market access and subsidies. Over the last several years, notification requirements have been tightened, generating information to judge the impact of STEs on trade flows. Thirty countries have notified the WTO of the existence of nearly 100 state trading enterprises. Because of differing interpretations and ambiguities in definitions, it is likely that not all STEs have been notified. STEs are generally used for politically sensitive commodities — grains, sugar, and dairy. This reflects the importance of domestic agricultural policy objectives as the *raison d'être* for this type of institution.

The prevalence of STEs in agricultural trade has generally been declining in recent years. While nearly 90 percent of both rice and wheat trade in 1970s was handled by state traders (Schmitz et al. 1981; Falcon and Monke 1979-1980) that share has fallen to between 33 and 50 percent today (Abbott and Young 1999; Young 1999). The decline in STEs is largely due to the impact of structural adjustment programs. The redistributive objectives of these agencies are costly, both in terms of domestic resources and foreign exchange, and were factors underlying the macroeconomic imbalances that led to

structural adjustment programs. Pressure from international institutions prompted reform of STEs. Many Asian countries avoided the pressures through better management of debt and foreign exchange and so less reform occurred in that region. To date, the WTO has had very little to do with the reform or elimination of STEs.

Countries have resisted the elimination of STEs since they are used to implement domestic policy. A common reform has been to permit private trading entities to coexist with public agencies. In some cases, importing STEs will continue to manage lower quality products targeted towards poorer consumers, while private agents handle trade for higher quality products. The coexistence of private traders with STEs is likely to lead to a reduction in the potential monopoly power of the state trader. However, the state trader may retain certain special privileges. Reform of STEs has also been accomplished through privatization of existing entities, so that the STEs have autonomy from the government. An example of this is the reform of the Australian Wheat Board, which will become similar to a producer cooperative, and may be required to operate without government subsidization.

F. Product Attribute Issues

Since the conclusion of the Uruguay Round, the adequacy of multilateral rules for measures that regulate product attributes has been called into question by new production technologies, new disease outbreaks, and new demands for agricultural regulation. Re-negotiation of the agreements covering product attribute regulations was not foreseen as part of the built-in agenda for the Agreement on Agriculture negotiations beginning in 2000, nor did any country formally propose reopening them during interim reviews by the relevant WTO committees. Yet interest in revisiting the rules has grown dramatically in the wake of events that has disrupted the consensus achieved in the UR. Nineteen negotiating proposals sponsored by seventy-four countries have addressed issues related to product attribute regulations in the first phase of the agriculture negotiations.

Several of the events propelling the renewed interest in these measures are well known. The emergence of GM products in agricultural markets and a series of BSE and FMD disease outbreaks in Europe have led to calls for the agreements to give governments more allowance in regulating risks. The EU, Japan, Switzerland, and other countries favor explicit recognition of the legitimacy of the *precautionary principle* and “other legitimate factors” in SPS policies, while countries such as the United States, Canada, Australia, and New Zealand favor current WTO rules.

Some countries are also urging greater accommodation of government efforts to respond to a range of consumer concerns unrelated to safety. These *demandeurs* would like the WTO to recognize explicitly the legitimacy of government regulations that either ensure specific attributes, or information about such attributes. The EU, for example, seeks to ensure that trade liberalization does not undermine efforts to improve animal welfare. The EU, Switzerland, Japan, and other countries have also proposed that mandatory labeling of credence attributes related to production practices, including genetic modification, should be explicitly allowed by WTO rules. WTO recognition of GIs for other products (e.g., cheeses, rice) is also advocated by some members. Several net exporting countries, including Australia, Colombia, and Argentina, have stated that they

do not accept any linkages between these issues and the outcome of the agriculture negotiations.

The large number of proposals and statements by developing countries that identify product attribute regulations as significant trade impediments has emerged as an important development in the current negotiations. In particular, developing countries report that anticipated market access opportunities have not materialized under the equivalence and harmonization provisions of the SPS Agreement. Beyond the question of whether the WTO agreements have provided effective solutions is the charge that the agreements are part of the problem. Some developing countries have claimed that the new obligations under the agreements (related to requirements for risk assessments, for example) are diverting scarce resources from investments needed to capitalize on the trade opportunities created by the AoA. These countries therefore have therefore proposed extended exemptions from selected provisions of the UR agreements in the current negotiations.

IV. Options for the Current Talks

Countries have made a range of proposals for dealing with various elements in the negotiations. Rather than discussing these by country, the following section presents a summary of the most important of these proposals grouped by topic.

A. Options for Improvement of Market Access

1. Tariff Cuts

There are many ways to cut tariffs, each involving a different distribution of benefits and costs. One technique is the approach used in the first five rounds of GATT negotiations of “request and offer”. Using the request and offer approach, participants try to balance their “concessions” against those that they seek from others. The problem with this approach is that highly protected sectors may be unaffected because they have nothing to “gain” in export markets. Request and offer has a tendency to focus on a few sectors. The result is that dispersion in levels of protection increases and the reduction in the average rate of protection can be modest.

Another form of sectoral negotiation is the “zero-for-zero” approach. Its advantage is the opportunity to increase market access for specific commodities with low levels of protection (Meilke, Wensley and Cluff, 2001). This approach is unlikely to open heavily protected markets and may even entrench protection, since there are fewer gains to be had in return for concessions in sensitive products. On the other hand, the approach does allow trade liberalization to proceed, to nearly free trade, in some sectors.

A final negotiating approach involves formula cuts in tariffs. Formula reductions can be as simple as an across-the-board cut of a given percentage in all tariffs over a given period, or as complicated as the negotiators’ imaginations allow. The approach can produce very different results depending on the formula adopted. There are two generic types of formulas: linear reductions that target the level of tariffs, and harmonization formulas that target both the level and the dispersion of tariffs (Wainio, Gibson and

Whitley, 2001). Linear reductions provide across-the-board cuts; harmonization reduces high tariffs proportionately more than low tariffs. The problem of tariff dispersion, including tariff peaks and tariff escalation, is best addressed through harmonization.²⁰

More complex tariff cutting schemes, which Josling and Rae (1999) refer to as a "cocktail" approach, can be developed by combining a reduction formula with a set of constraints, such as a ceiling on the tariff level and the elimination of "nuisance" tariffs – those below a specified level.²¹ Harmonization formulas are flexible enough that negotiators can achieve any degree of tariff liberalization they wish. Given the tariff profiles in agriculture, a Swiss formula that allows for a ceiling tariff and the elimination of nuisance tariffs, would seem to be preferable. If this is not possible, the minimum that should be accepted is a replication of the UR cuts. By contrast, a "request and offer" approach would not be desirable.

Any formula designed to reduce average tariff levels requires negotiators to specify a base period, and an averaging formula. In the URAA, industrial countries bound most agricultural tariffs at applied 1986-88 rates. Many developing countries established bound tariffs that were well above applied rates. One option would be to start the next round of reductions from applied, rather than bound levels.²² This would remove the discretionary element in the current system of bound tariffs. It would reward countries that set their tariffs close to the bound level, and penalize countries with relatively open markets that rely on stabilization schemes such as price bands. The first group primarily includes developed countries, while the second group primarily includes developing countries.

A second option would be to use tariffs from the final year of the Uruguay Round cuts as the base. However, most WTO members want to start from existing bound rates, since countries that have unilaterally reduced tariffs beyond those agreed in the URAA would otherwise not receive credit for their actions. Establishing a new base for tariff reductions would be quite controversial; providing credit for reforms undertaken since the UR would complicate the process.

A third and less controversial option would be to use the same base selected for the Uruguay Round (Tangermann 1997). A further extension would be to cut tariffs in roughly the same manner as in the URAA. This option would emphasize the continuity of the liberalization process and avoid the difficulty of establishing a new base. In the Uruguay Round, members exploited the simple average 36 percent overall reduction by applying the minimum 15 percent reduction to sensitive products and making large cuts

²⁰ The best-known formula is the Swiss method, which was applied in the Tokyo Round. This formula is designed to achieve deeper cuts in high tariffs and to address the problem of tariff peaks. The formula is $T_j = aT_0 / (a + T_0)$, where T_0 is the initial tariff, T_j is the new tariff and a is a parameter that determines the depth of cut. The reduction parameter, a , used in the Tokyo Round was 16, but this reduction method was designed for initial tariffs that were less than 50 percent (Laird 1998). With the parameter $a = 16$ a tariff of 350 percent is reduced to 15 percent; with $a = 60$ the reduced tariff is 51 percent; with $a = 140$ the reduced tariff is 100 percent.

²¹ Wainio, Gibson, and Whitley (2001) evaluate a number of alternative formulas.

²² This option has been suggested by the US for both the WTO and the FTAA tariff negotiations.

in small tariffs. The avenue of continuing to protect sensitive sectors with minimal cuts has become more difficult because there are fewer low tariffs to trade-off in the overall average. However, this approach still allows countries to avoid liberalization for some sectors. Designing special rules to decrease the dispersion in tariffs resulting from a repetition of the UR procedures would also complicate the process. If all nuisance tariffs were eliminated without being counted in the overall reduction formula, the approach is much more promising and avoids the necessity of calculating *ad valorem* tariffs as for harmonization formulas.

Box 2: Options for Tariff Cuts

- Employ harmonization (Swiss) formula that establishes ceilings on tariff rates
- Bring down average agricultural tariffs to no more than an agreed multiple of the average tariffs for imports of manufactured goods
- Eliminate nuisance tariffs
- Initiate cuts from applied rates or from the final year of the Uruguay Round cuts as base
- Eliminate complex tariffs and convert to *ad valorem* equivalents to maximize transparency
- Ensure that any zero-for zero sector agreements does not entrench protection in sensitive sectors

Having selected a base period for tariff reductions, another problem is to determine the appropriate averaging technique to aggregate across commodity groups. The choice of technique is important for establishing overall tariff reduction commitments. In past rounds, targets for the overall reduction of tariffs on industrial products were set as import-weighted averages (Laird 1998). This approach was not used for agriculture, where simple averages were used to determine the depth of cut.²³ Each of the averaging methods: simple average, trade-weighted, and consumption and production weighted aggregation techniques has limitations. The minimum 15 percent reduction for each tariff line was intended to solve the problems associated with simple average weighting, but ultimately allowed WTO members too much flexibility - it was used to avoid meaningful tariff reductions for sensitive products. An alternative way to mitigate the problem of a reduction target based on a simple average is to establish a ceiling rate for any tariff.

Simplification of the tariff structure is a final important issue. The elimination of complex tariffs (i.e., combinations of specific and *ad valorem* tariffs) should be pursued to increase transparency. The use of a single type of duty, the *ad valorem* tariff, would maximize transparency.

²³ Import weights were not used because many markets involved little or no trade because of the prevalence of non-tariff barriers.

2. Improvement of Operation of TRQs

What options are open to countries as they negotiate on TRQs? Two broad suggestions are offered here. First, the negotiators should agree that TRQs are a transitional mechanism that will eventually be eliminated. Second, the negotiators should make sure that all countries abide by the same set of transparent rules in applying TRQs.

One promising strategy for eventual elimination is to replace arbitrarily awarded market access under TRQs with auctions, and to use the auction prices to establish a true tariff equivalent. This could then be used to set the initial, bound over-quota tariff, which would gradually be reduced. An alternative approach would be to establish resale markets for quota rights. This would avoid the need to develop a potentially expensive bureaucratic structure; if resale markets were monitored that would provide information on the true tariff equivalents for the products traded. These options are appealing because they would minimize disruptions to markets by gradually reducing trade barriers, while at the same time providing meaningful market access opportunities. However, the approach depends on the feasibility of auctions or resale markets and might require a long implementation period. Tariff equivalents may vary considerably from year to year and this might lead to disputes over the choice of an appropriate base period.

Even if the best long run solution is to eliminate TRQs, exporting countries that enjoy preferential access under TRQs may not agree to their elimination. Operating on one component of the TRQ is an alternative approach. A steady expansion of the minimum access commitment would eventually eliminate the trade effects of the TRQ. Progressively reducing the over-quota tariff would achieve the same end. Conversely, reducing the in-quota tariff may not improve market access.

If TRQs are not eliminated, tariff reductions only address two of the TRQ's three components. Liberalization of the minimum access commitment addresses the third component; disciplines on TRQ administration address a closely related concern. Josling (1998) and Anderson (1999) advocate expanding the size of the minimum access commitment as the only practical method of overcoming the entrenched protection inherent in the TRQ system. Expanding the minimum access commitment is useful when imports equal the quota, indicating that there is excess demand for the import. Also, quota rents would be reduced.²⁴

Rents may increase when a non-binding constraint is relaxed, for example, by lowering the in-quota tariff when the quota is binding. Quota rents are important because of their potential to bias trade. The rationing of limited supplies and the distribution of rents are addressed through TRQ administration, which is judged by two criteria: quota fill and bias in the distribution of trade. Market-based allocation methods such as quota auctions and unrestricted re-sale of quota rights capture quota rents and remove the incentive for biased trade. Determining the best allocation method to ensure maximum fill when there is excess demand at the in-quota tariff is more challenging. Complete fill should occur as long as economic rents exceed transactions costs. Administered techniques – historic access, state trading enterprises, etc. – may be less complex than auctions, and may

²⁴ With an inelastic demand rents will decline as quota is increased, but with an elastic demand quota rents will increase as the import quota is expanded.

involve fewer transactions costs for importers/exporters. However, these methods are not responsive to market conditions and may involve less transparent transactions costs, such as those due to political preferences. Unfortunately, the best choice of quota administration method, in the face of transactions costs, is specific to the product that is being traded.

Box 3: Options for Improvements in TRQs

- Establish the level of product aggregation and a common base period for minimum access commitments
- Expand access to a common percentage of domestic consumption with no exceptions
- Establish transparent procedures for quota allocation with auction or resale markets in import quota rights
- Apply tariff reductions to both in-quota and over-quota tariffs.

There is general agreement that the base period for the minimum access commitments should be updated and made uniform across countries. In the URAA the "guideline" for minimum access was 3 percent of domestic consumption, rising to 5 percent of domestic consumption. However, many countries did not apply this guideline. Hence, a new set of domestic consumption figures and current access commitments, as a percent of domestic consumption, should be developed so that all countries are working from a common base for minimum access commitments. Simultaneously, negotiators will have to determine the level of product aggregation to which these commitments will apply.

3. Special Safeguards

In almost all WTO members, some sectors are politically sensitive, and members reserved the right to take action quickly through the Special Safeguards (SSG) of the Agreement on Agriculture if imports threaten domestic producers. The first issue is whether the SSG should be continued. One interpretation of the URAA is that the safeguard will continue as long as the reform processes continues, and so will continue if further reform is undertaken.

Opponents of extending the SSG point to the "emergency safeguard" (Article XIX) provisions that allow members to take action if increased imports cause or threaten to cause serious injury to a domestic industry. They argue that this safeguard is sufficient for agricultural trade. They see the elimination of SSG as an important step towards subjecting agricultural trade to the same rules that apply to other goods.

A further view is that SSG is essential for achieving agreement on further trade liberalization. The political reality of agricultural reform in many countries is that stakeholders demand some discretionary control of trade flows. They need assurance that

action can be taken, if necessary, to counter large, price-depressing inflows of products. Given that a SSG is inherently distorting, accepting the mechanism as a compromise to obtain further tariff liberalization requires rules to ensure that SSG does not become more distorting than the measures it replaces. To this end, providing smaller offsets (tariff increases) for a fall in domestic prices, or shortening the period for the quantity trigger would tighten the current criteria. Negotiators should attempt to keep the mechanism as transparent as possible, so that affected parties are provided adequate notification and information about additional duties. The use of the SSG should be time limited and regulated, with renewals and extensions judged by a technical committee comprised of a third party representative, and possibly involving an injury test.

Proponents of an agricultural SSG point to the level of transparency that is achieved if nations use a safeguard rather than price bands – reference prices and applied tariffs that vary with changes in import prices (Josling and Rae, 1999). Nations would retain the right to take prescribed actions, but would forgo the use of trade distorting policy instruments, such as the EU reference price system. This use of an agricultural SSG could contribute significantly to a compromise in the negotiations: transparency of action is the cost of maintaining discretionary control of imports.

Box 4: Options for Reforms on Special Safeguards (SSG)

- Consider eliminating SSG and use WTO safeguards instead
- Make SSG available to all commodities and countries uniformly, including seasonable and perishable products
- Limit tariff increases and the period of application of SSG, with renewals and applications subject to review under the WTO
- Make SSG conditional on forgoing other variable tariff schemes

B. Options for Improvement of Export Competition

1. Export Subsidies

The inclusion of disciplines on export subsidies was a major accomplishment of the URAA. Some argue that base period levels may not have been representative of subsidized export flows in the early 1990s, and may have actually encouraged an increase in subsidized exports during the implementation period. However, the initial bindings encouraged countries, such as the EU, to sign the URAA. One option available for the current round is to initiate cuts in permitted expenditures and volumes from the final 2000–01 bound levels. Some economists have argued for additional cuts at the same pace of the URAA implementation period. Though export subsidies would still exist, such cuts would require significant policy reforms in the countries that employ export subsidies, and would be a major step towards export subsidy elimination.

The use of both value and volume commitments constrains export subsidies in times of both high and low prices. When world prices are low, the value limit becomes more

constraining because the wedge between the domestic support price and the competitive export price becomes larger. Volume limits prevent exports of excess supply when there are low domestic prices. When world prices are high, the value constraint becomes less binding but the volume constraint can still be effective. Therefore, limits on both value and volume weaken the ability of export subsidies to maintain fixed internal price supports. Further restrictions on export subsidies are likely to encourage reductions in the domestic price supports that encourage surplus production.²⁵

One proposal that has been promoted and which affects export subsidy disciplines is the so-called “zero-for-zero” option. Under a zero-for-zero agreement, all members would eliminate support, including export subsidies, for a single commodity or a group of commodities. Based on WTO notifications, the only commodity group for which a zero-for-zero program is unlikely to undermine export subsidies is oilcakes. No country notified subsidized exports of oilcakes from 1995 to 1998. Other commodities where zero-for-zero would be feasible in terms of export subsidies would be cotton and oilseeds. However, countries may be reluctant to give up the option of subsidizing their exports in the future. Unless countries are given the opportunity to select one or two commodities for which they would be willing to give up the use of export subsidies, a zero-for-zero program would most likely not be viable. The zero-for-zero option is unlikely to be attractive to the European Union, the major user of export subsidies.

Box 5: Options for Reforms in Export Subsidies

- Agree to the elimination of all export subsidies by a date certain
- Further reduce bindings on the volume and value of export subsidies
- Consider rules to prevent circumvention (such as EU component subsidies)
- Eliminate the ability to “rollover” unused subsidies to future years
- Revisit the definition of export subsidies to account for consumer-financed subsidies and cross subsidization across commodities

2. Export Credits

Research on officially supported agricultural export credits has raised several issues. These relate to the extent to which export credit programs contain subsidies, the extent to which they distort trade, and how disciplines on credit programs would limit distortions. Understanding these issues should condition negotiations on export credit programs.

The estimated subsidy value of existing programs is relatively low. Only for U.S. programs are subsidy values above four percent, and credit terms longer than one year. In all cases, the relatively low subsidies are likely to create small trade distortions. Evidence

²⁵ Some countries argue that market promotion activities should be subject to export subsidy disciplines. However, Article 9, Section 1d exempts widely used export promotion and advisory services from export subsidy reduction commitments.

from the literature suggests that programs may create additional demand, and to the extent that this is true their negative impact on competing exporters is likely minimal.

Disciplining officially supported export credit programs is more likely to be accomplished by limiting the term of loans offered, and by constraining government budgetary outlays, rather than by constraining program parameters such as minimum interest rate requirements. Constraining interest rates or other program parameters risks interfering with commercial relationships, may negate the value of a program to the importers, and limit additionality.

Difficult issues arise where credit programs overlap other forms of subsidies, such as food aid. Special and differential treatment of credit programs for developing countries is mandated in the Uruguay Round Agreement. This could more effectively target liquidity constraints and generate additional demand.

Box 6: Options for Restraints on Export Credits

- Limit the term length of export credits
- Limit government budgetary outlays for export credits
- Consider differential treatment for credits provided to developing countries

C. Options for Reform of Domestic Support

Country proposals suggest that domestic support is likely to be among the most contentious elements of the agricultural negotiations. Proposals highlight a range of issues, including reductions in aggregate support (including definition and criteria for exempt policies; consideration of inflation and exchange rate changes; the role of *de minimis* provisions; and total versus product-specific AMS commitments); the accommodation of “non-trade” concerns; the role of the Blue Box; limits on Green Box subsidies; the role of the Peace Clause; and special and differential treatment.

One of the challenges for the negotiations is to identify ways to reduce trade-distorting domestic support while providing countries with the flexibility to achieve important societal goals. The urgency of this issue will increase as the amount of support allowed within the Amber and Blue Boxes declines. Criteria must be refined to provide clearer definitions of acceptable minimal-trade-distorting domestic policy measures that allow countries to pursue important societal objectives, such as those concerning environmental standards, rural development, food security and poverty alleviation.

1. Further Reductions in AMS

The URAA placed limits on individual countries’ total AMS and specified reductions, resulting in a final, bound support level. Issues for the current negotiations are how much further to reduce those levels, and whether or not to use the bound support level as a base for further reduction. The bound AMS varies greatly among countries, with most having a zero commitment but some having high levels in relation to the size of their agricultural

sectors. In addition, negotiators will have to consider the method of reductions. Should support be reduced *by* a given amount or *to* a particular level? Reducing support by a given amount provides advantages to those countries with currently high levels of support. Reducing support to a particular level would result in a more level playing field among countries, but impose greater adjustments on countries with high levels of support.

The current *de minimis* rules specify the level of support in developed and developing countries that is exempt. Negotiators will likely consider whether such exemptions should be retained. It could be questioned why *de minimis* thresholds are needed in the AMS rules but not in other parts of the URAA. Such a provision does not save time and effort: calculating and monitoring of the AMS is still needed to justify a *de minimis* claim. If this provision is maintained, the issue is to determine whether and by how much (or to what level) the *de minimis* threshold will be reduced. Some countries have proposed that developing countries should be allowed to increase the level of support provided under the *de minimis* provision.

AMS commitments and levels are reported in nominal terms. High inflation or fluctuations in exchange rates distort the evaluation of support levels. Negotiators should consider the development of criteria that account for inflation or exchange rate fluctuations in determining a country's AMS level.

Since the URAA was implemented, a number of countries have shifted significant portions of their domestic support from the non-exempt category into the Green and Blue Box categories. One issue that this raises is whether all domestic policies currently categorized as exempt truly fit the criteria of the current agreement. The next agreement may seek more specific criteria to determine the status of domestic support policies. Specifically, the issue of decoupled payments must be addressed and appropriate criteria developed.

As the Agreement currently exists, countries have the flexibility to adjust the level of support among products in the Amber Box, provided that the Total AMS does not exceed their commitment. Setting AMS limits on a product-specific basis would increase the discipline of the Agreement.

2. Future Role of the Blue Box

The intent of the Blue Box category in the URAA was to make it easier for the EU and the U.S. to meet their domestic support reduction commitments. Some argue that the Blue Box was transitional and should be phased out, thus encouraging countries to adopt measures that fit Green Box criteria. Blue box payments are not included in the AMS calculation and are exempt from reduction commitments. However, there exists the possibility of output and trade impacts from Blue Box policies, and hence a desire by exporting countries to discipline these. The key issues concerning the Blue Box are whether it should be eliminated, and if so, at what rate.

3. Limits on Green Box Subsidies

The URAA placed no limits on the level of support that can be provided within the Green Box framework, which is supposed to include measures that have no, or at most minimal, trade-distorting effects or effects on production. The two basic criteria are that support

must be government-funded (not involving transfers from consumers), and must not have the effect of providing price support to producers. A number of policy-specific criteria and conditions also apply. However, the less-than-precise nature of the criteria has left considerable room for interpretation on allowable Green Box policies. Beyond the clarification of acceptable Green Box policies, several countries have called for limits to be imposed on the amount of support provided. While limiting Green Box expenditures will be a contentious issue, an area of compromise could involve improved definition of policies that have no, or at most minimal, trade-distorting effects or effects on production.

4. Role of the Peace Clause

The peace clause provides an incentive for countries to shift domestic policy instruments towards the Green Box category in order to eliminate the threat of countervailing duties and other actions. One question concerning the future of the peace clause is the form that it should take to encourage the greatest shift toward qualifying support. Should the clause be permanent or of limited duration? Should it only cover Green Box policies or include other support? If the peace clause were allowed to expire, would this eliminate much of the incentive to shift from non-qualifying to qualifying support categories? The outcome concerning the peace clause and its optimal form will depend on changes that take place with respect to the various categories of support.

Box 7: Options for Restraints on Domestic Support

- Reduce AMS by no less than the UR cuts and consider setting limits on a product-specific basis to a particular level
- Assess relevance of maintaining *de minimis* provisions, especially for developed countries
- Impose constraints on Blue Box expenditures and clarify provisions on production limiting requirements
- Establish clearer criteria for acceptable minimally-trade-distorting instruments in the Green Box
- Consider eliminating the Peace Clause or confining its provisions to Green Box Policies

D. Options for Food Aid

The most prominent food aid program that operates on a concessional basis, using subsidized credit, is the U.S. PL 480 Title I Program. This has the stated goal of promoting U.S. agricultural exports. Negotiators should consider moving Title I from food aid to export credits. As mentioned in the discussion on export credits, such programs are also mandated to provide terms favorable for least-developed and net food-importing countries. Negotiating the PL 480 Title I in the context of export credit

negotiations may meet both donor and recipient country desire to eliminate unclear distinctions between food aid programs and export credit programs.

A tighter definition of food aid is not likely to make a significant difference to the degree to which food aid disrupts world markets (unless it ensures additionality). However, if all donors were to abide by common definitions of food aid, it might be easier for agricultural exporters to tolerate a small price-depressing effect associated with food aid. If the criteria adopted were successful in targeting food aid to countries in need, those countries would benefit from a more effective use of available supplies.

Box 8: Options for Reform in Food Aid

- Identify transactions that are not acceptable as food aid; subject these to strict notification and consultation requirements and to overall limits
- Improve notification protocols under the Consultative Committee on Surplus Disposal (CSSD) and make this information easily accessible
- Exercise caution in new disciplines for food aid that could result in a reduction of overall food aid availability

Food aid may at times be used as an export subsidy to reduce unwanted surpluses. The most explicit form this takes is when aid is tied to the requirement that the recipient source its imports from the donor. The URAA prohibited this. However, the Agreement did not discipline more implicit subsidies, such as those for which disciplines are being sought by the European Union. Adequate (increased) levels of food aid guaranteed in advance by donors and delivered through the World Food Program would solve some of the problems. The WTO might also want to consider establishing a Food Financing Facility similar to that proposed by several developing countries that would provide a short-term safety net for importing countries facing difficulty in financing normal commercial requirements of basic foodstuffs. Such a fund might increase the confidence of countries facing adjustments because of a more liberal agricultural trading environment.

But recognition should also be given to two immediate difficulties facing the discussion of food aid in the WTO. First, disciplines for food aid need to be discussed in a venue that recognizes the tradeoffs between the adequacy of food and the need for disciplines on the export subsidy element of food aid. Secondly, food aid issues need to be discussed in a venue where food aid recipients share power over the decisions. Neither the WTO, nor existing multilateral institutions concerned with food aid, appear to fulfill both requirements.

E. Options for Reforms in State Trading

A review of the various negotiating proposals indicates that the definition of State Trading Enterprises is in urgent need of clarification. Concerns have been raised about the monopoly and monopoly power exercised by these entities. Similarly, their ability to use price-discrimination among markets and to engage in price pooling are being challenged in the WTO, especially in the face of a lack of transparency in the operations

of STEs. In many countries, STEs are charged with achieving a broad set of domestic policy goals. To the extent that domestic constituencies support these goals, there can be high political costs for national governments in abandoning these institutions.²⁶ In some cases the outcome of the politically costly process of reform has been the implementation of new methods to achieve the same domestic policy goals. In other cases, private monopolies have entered the market, such that concerns about market power, transparency and price discrimination have not been alleviated. Rents are captured by private firms, and are not passed on to producers.

Box 9: Options for Reforms in State Trading

- Consider market power issues in the context of broader competition policy
- Evaluate if the current WTO dispute resolution system is adequate to investigate violation of commitments by STEs
- If further disciplines are enacted, consider differential treatment for developing countries

F. Options for Special and Differential Treatment

One of the lessons of the Ministerial Meeting in Seattle in 2000 is that the developing countries are unwilling to participate in another round of trade negotiations in which their views are not fully considered (Stiglitz, 2000). It is important to stress that the developing countries are not a homogeneous block. Several developing country food exporters are members of the Cairns Group and as such, share that group's aim of rapid agricultural trade liberalization. Conversely, developing country food importers remain skeptical of the benefits of opening their domestic agricultural markets. However, all developing countries share three major concerns with the current trading system: the structure of the WTO; the perceived lack of benefits from the UR negotiations; and that special rules and disciplines for developing countries must be put in place during the current round of negotiations.

Developing countries dominate the membership of the WTO; since the conclusion of the UR roughly 40 new developing country members have been added. Despite their majority position, most developing countries feel that important debates and decisions at the WTO take place without their full participation. As stated by the former U. S. Trade Representative, Ambassador Barshefsky, following the Seattle Ministerial: "the WTO has outgrown the processes appropriate to an earlier time...We needed a process which had a greater degree of internal transparency and inclusion to accommodate a larger and more diverse membership." The WTO has responded to some of these concerns by making most WTO documents publicly available, and by providing technical assistance and training for developing country representatives. It is not the mandate of this paper to

²⁶ In the Canadian case, support exists on the part of some producers for elimination of the Canadian Wheat Board.

discuss WTO institutional reform, but this remains a key issue in making developing countries an integral part of the decision making process.

Many developing countries feel the benefits promised to them as a result of the UR agreement have not been forthcoming. Their list of grievances is long and only a partial review is provided here. First, with respect to market access they feel they have not benefited to the degree expected from the liberalization of developed country markets for agriculture, clothing and textiles. Further, they fear that when they do become competitive in developed country markets, they are subjected to anti-dumping actions that are generally too costly for them to block effectively. They also realize that because of the UR agreement, their domestic markets continue to face competition from agricultural products exported by developed countries with the aid of export subsidies. In addition, their domestic support for agriculture is largely constrained to *de minimus* levels as a result of the URAA, while developed countries continue to pour huge sums of money into their domestic agricultural sectors through the amber, green and blue boxes. Poor developing countries feel they have no chance to compete effectively in agricultural markets against the deep pockets of the rich and powerful countries of the world. Finally, developing countries fear the inclusion of environmental and labor standards in trade agreements.

For many developing countries, border measures are the only policy instrument available to provide income support to their farmers. Unlike developed countries, taxpayer funded support measures are not an option given budget realities. This provides one rationale for allowing developing countries to retain some water in their tariffs and to have access to a special agricultural safeguard mechanism.

These are the concerns that negotiators face as they attempt to develop rules for special and differential treatment of developing countries. Many of the poorest developing countries have 60 percent or more of their labor force in agriculture, and agriculture often accounts for more than 40 percent of their GDP. However, developing countries have a large stake in trade liberalization given that 43 percent of developing countries are net agricultural exporters, including 28 of the world's poorest countries (McCalla, 2001).

Preferential treatment in market access involves the same issues as broader market access. The level of tariffs and their dispersion should be dealt with using a harmonization formula. However, the effects of liberalization will be asymmetric for developing countries since they will retain greater levels of protection while receiving preferential access to developed country markets. Harmonization formulas, like the Swiss formula, could be used with different parameters for liberalizing both developing and developed country tariffs.

With respect to market access, the EU recently approved a proposal to eliminate tariffs and quotas on all products, except arms, from the world's 48 poorest countries. The adoption of this policy by the EU will put considerable pressure on other developed countries to follow suit. In addition, developing countries other than the 48 included in the EU scheme are sure to press for similar treatment.

Developed countries should be prepared to grant developing countries major tariff concessions on all agricultural products, including those that are import sensitive, during this round of negotiations. In return, developing countries should agree to liberalize their

own agricultural markets, and a longer transition period for tariff reductions could be provided. Developing countries should agree to pursue their non-trade concerns using instruments that are consistent with less border protection. This approach may require additional financial aid from developed countries, and perhaps even new international institutions. However, the provision of some additional financial support to address non-trade concerns in developing countries is a small price to pay for obtaining meaningful reductions in agricultural trade barriers.

The creation of a special developing country safeguard may be a consideration for the large number of developing country products for which the bound rate substantially exceeds the applied tariff. Special treatment in terms of bindings should be addressed with a safeguard measure and not through the tariff system.

Box 10. Options for Special and Differential Treatment

- Continue to promote preferential access for developing countries through preferential tariffs in developed countries
- Reduce tariffs in developing countries using a harmonization approach, but allow a longer transition period for reductions
- Include smaller reduction commitments on domestic support, a higher *de minimis* level, and longer implementation period
- Add to the specific green box criteria for WTO members who qualify as developing countries
- Address developing country concerns about trade liberalization through increased technical assistance and financial aid

Developing countries have been afforded special and differential treatment under the URAA for domestic support. These include a smaller reduction commitment, higher *de minimis* level, longer implementation period, and exemption for the least developed countries from all reduction commitments. The continuation of these special and differential treatments seems appropriate. In addition to determining what special and differential treatment will be granted, the current negotiations should develop specific criteria on which WTO members will qualify as developing countries. The application of special and differential treatment to transition economies will also need to be addressed.

G. Options for Further Action on Product Attributes

The existence of trade restrictions based on product attributes has emerged as an important issue in the WTO. The current round of agriculture negotiations has been characterized as one in which governments are seeking additional latitude, discipline, or clarity with respect to their multilateral commitments regarding product attribute regulations. Proposals that seek additional latitude for policy interventions could potentially unravel the modest regulatory reforms of the Uruguay Round. To the extent that the negotiations provide more latitude for developed countries to respond to revealed

or perceived domestic demands for product standards, the goal of the WTO should be to ensure that this latitude does not limit trade. Some of the calls for additional regulatory latitude appear to be designed with other social goals in mind, and to this extent are disingenuous when cast as questions of regulatory policy related to product attributes. Developing countries have also requested additional latitude in fulfilling their obligations under the agreements. These concerns are best addressed with increased technical assistance that promotes their integration into the world economy, rather than special and differential exemptions that delay it.

Proposals to strengthen current WTO rules by requiring proportional policy responses to risks, limiting deviations from international standards, or otherwise tightening the criteria for a legitimate product regulation could move countries closer to optimal economic policies, but at the cost of some political capital. Debate over regulation that limits trade is usually part of a larger contest over all regulation that is often vigorously debated *within* sovereign states, let alone between them. Within this larger debate, economics recommends the merit of market-based solutions over rigid command and control rules, careful assessments of the costs of regulation, and weighing the costs against the benefits of a proposed measure. But because product attribute regulations in many instances address market failures in order to achieve greater consumer welfare, it is one area where consumers do not gain unambiguously from trade. This creates a different political economy for WTO negotiations: tighter disciplines on product attribute regulation will meet with political resistance from some consumer groups, in addition to protected producers.

The case for clarifying current multilateral rules, rather than changing them, is strong. There is widespread agreement that the promise of some innovative Uruguay Round initiatives, such as equivalence and regionalization, has not yet been fulfilled. The causes of failure need to be diagnosed, perhaps with the assistance of the international standards organizations, before effective remedies can be prescribed. The “new issues” raised in many proposals also merit further debate. Simply dismissing as protectionist any initiative to discuss such issues such as the regulation of production and processing methods or labeling regimes not only hardens opposition to further trade liberalization among some constituency groups, it also squanders an important opportunity to examine how trade can contribute to providing consumers with desired products in the most cost-effective manner. The whole attributes/trade debate could constructively be turned to shift the focus from expanded trade as a *threat* to desired product attributes to expanded trade as a resource efficient means to *achieve* those attributes. Debate within the standing SPS, TBT, and Trade and Environment Committees, rather than the agricultural negotiations *per se*, should be considered: this option would capitalize on the expertise in these committees, reduce the likelihood of divergent solutions for the regulation of agricultural and industrial products, and minimize diversion from further liberalization of traditional trade barriers which still significantly distort agricultural markets.

Box 11. Options for Regulations on Product Attributes

- Focus future international efforts on implementing the Uruguay Round reforms related to equivalence and regionalization
- Capitalize on the expertise of the standing SPS, TBT and Trade and Environment Committees to clarify existing multilateral rules related to new cross-cutting issues such as mandatory labeling of production processes and the precautionary principle
- Provide technical assistance to developing countries to strengthen their regulatory regimes so that they can both gain greater access to foreign markets for their products and fulfill their obligations under the agreements

Progress on these issues will depend on abandoning the polarizing debate over which objectives are legitimate, and instead focusing on the requirement that policy regimes provide the least trade restrictive means for achieving a stated objective. A useful first step for those who propose increased product attribute regulations would be to identify, for example, how production and processing method regulations can be formulated so that *all* producers have the opportunity to compete in markets. Regulatory proposals that advance measures not coincidentally favorable toward domestic producers, or that include technical assistance for developing countries to enter marketing channels, or that consider independent, third-party certification, could help dispel suspicion that consumer concerns are addressed only when it is politically expedient to do so. Those who favor less national regulation about product attributes are likewise challenged to offer explanations and examples of when and how the market, or the market in tandem with limited government intervention, provides optimal (and often more agile) solutions to matching product availability with evolving consumer preferences. Refusal to engage in this debate will not forestall consumers' interest in certain product quality attributes; indeed, those who wish to export to some markets have already found that the requirements of private firms exceed those found in WTO negotiating proposals.

V. Negotiation Outcomes

The packaging of possible outcomes in the agricultural negotiations has to reflect balance in at least four different dimensions. First and foremost, it has to meet the major aspirations of both developed and developing countries. The events at the WTO meeting in Seattle showed that developing countries are not about to agree to a negotiating conclusion that ignores their interests. Proposals by the developing countries make explicit their concerns and those in the developed world have indicated a willingness to take them into account. But an acceptable package will need to have substantial market access in products of interest to developing countries; recognition of special development needs in domestic policies; some allowance for safeguard action in the event of market disruption; and a stronger commitment to action on food security in times of high world

prices. In turn, developed countries will expect full involvement by developing countries in the market opening commitments and some further restrictions on the activities of state trading importing agencies. This package would be easier to achieve in the context of a round that extends beyond agriculture because other benefits such as improved market access in the textiles area could be included, along with better access for developed countries to the markets for manufactured products in the developing countries.

Second, the package has to be balanced between importing and exporting countries. In spite of the restraints on export subsidies agreed in the Uruguay Round, the feeling is widespread that exporters have had to make less painful adjustments as a result of that agreement. Exporters may feel that the major problems of agricultural trade are the fault of protectionist importers, but the importing countries have always claimed that their own policies reflect the need to be protected against erratic world prices that are depressed by the activities of the exporters. Whatever the merits of these arguments, it is unlikely that a deal could be struck on this occasion if the only changes in export policy were further reductions in the EU's export subsidies. Australia and New Zealand may be excused from "pain" in the final package, but the Canada and the United States will not be able to escape so lightly. The EU is also a major exporter, but in many ways acts as an importer of temperate zone commodities. A change in trade policy strategy from a defensive to an offensive approach has been slow in the EU. There are signs that the EU is finally beginning to argue for open markets rather than insist on the right to keep these markets protected. A key to the current talks may be the extent to which this attitude is manifest in the EU's behavior in the negotiations.²⁷

A third aspect of the package is the balance among commodities. It is well understood that the Uruguay Round left some commodities, notably sugar and dairy products, virtually untouched. In contrast, serious discussions were held on virtually free markets for oilseeds. Some countries are in favor of trying again with zero-for-zero agreements, which could have the effect of exacerbating distortions across agricultural markets.²⁸ The question is whether this round of talks can conclude without significant liberalization in dairy and sugar markets. The answer is shrouded in the domestic politics of the EU and the U.S., but the Cairns Group could also have a say in this. Australia and New Zealand have a strong incentive to see that dairy trade is not treated lightly in this round. Dairy markets have shown some signs of recovering from the disarray caused by unrestricted export subsidies, but they are still distorted by high tariffs. Further domestic reforms by the EU and a continuation of the moves toward a more liberal policy on dairy products in the U.S. could set the scene for a significant degree of liberalization in this sector.

The same may not be true in the sugar market. Low cost suppliers, particularly Australia and Brazil, will push hard for sugar to be included in the tariff reductions in the round. However, some developing countries benefit from preferential access for this product into EU and U.S. markets, which complicates negotiations on market access.

²⁷ It is ironic, if not inexplicable, that the EU country with the most defensive position with respect to the talks (France) is also one of the main agricultural exporters in the EU. Presumably the change of heart mentioned here is largely dependent on changes in French policy, which could come after the next election.

²⁸ See Josling and Rae (1999) for a discussion of the drawbacks of sectoral imbalances.

The fourth element is balance among the various parts of the package. The balance among instruments is difficult to define. Clearly some of the measures are connected: we know that lower tariffs will restrict the ability of countries to use export subsidies, reduce the potential trade diversion impacts of free trade areas and cut the quota rents from TRQs. But there are also links between the use of safeguards by importing countries and the control of export subsidies. It is likely that the market access and export competition components will have to be considered as a whole and a reasonable balance achieved. Less obvious is the connection between domestic support and product attributes. One deals with disciplines on the attempt by countries to pursue domestic policy in rural areas, and the other with disciplines on domestic quality and safety regulations. In each case, the issues are the extent to which the domestic policies can be reformulated to have less impact on other countries, and the way in which one can prevent capture of these domestic regulations by those seeking to protect domestic producers. Again, a balance will have to be sought which represents a domestically acceptable set of international constraints.

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