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Farm Support Programs and World Trade Commitments

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Geoffrey S. Becker
Specialist in Agricultural Policy
Resources, Science, and Industry Division

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Summary

The 1994 Uruguay Round Agreement on Agriculture (URAA) obligates members of the World Trade Organization (WTO) to make changes in their domestic farm policies to facilitate more open trade. Domestic programs deemed, at the time, to have the greatest potential for stimulating too much production, and thereby distorting world trade in various agricultural commodities, were subject to annual spending limits. (Other important provisions commit countries to reduce farm export subsidies and to lower agricultural import barriers.)

The UR commitments made by WTO members constrain their flexibility and spending choices whenever they consider ways to assist agricultural producers. As a WTO member and signer of the Agreement, these constraints affect the United States, which was a leading voice in calling for agricultural trade reforms and reductions in domestic supports. Since then, Congress, from 1998 through 2000, passed a succession of bills appropriating a total of more than \$17 billion in *ad hoc* assistance, over and above benefits already authorized under the omnibus 1996 farm law, to help producers cope with poor market conditions. U.S. officials recently classified the first installment of these payments as potentially trade distorting.

Despite the high levels of support (relative to previous periods during the 1990s), the United States so far appears to be within its prescribed annual spending limits. And, defenders of current U.S. farm policies point out that the 1994 Agreement, for example, has permitted the European Union (EU), a chief U.S. export competitor, to spend far more than the United States on domestic farm aid. They argue that so long as the EU and other foreign countries heavily subsidize their farmers, a “free world market” in agriculture is illusory, and U.S. farm aid should not be singled out for criticism.

In fact, domestic farm support spending by major agricultural traders generally had been increasing in recent years, according to analysts, raising the question of how effective the UR agreement has been in reducing trade distorting domestic subsidies worldwide. With a new round of negotiations now under way to continue the process of agricultural trade reform, WTO members are offering a divergence of viewpoints on how to handle domestic farm supports. These range from countries that will seek continuing, and deeper, reductions in spending, to those that are likely to defend their internal subsidies as necessary for various national policy reasons.

Congress is now debating reauthorization of omnibus farm legislation, as most commodity price support provisions expire in 2002. Because of the interrelationships between trade and domestic support policies, lawmakers are interested in what the Agreement on Agriculture stipulates with regard to domestic supports, and how not only the United States but also other countries are meeting their Agreement commitments.

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Farm Support Programs and World Trade Commitments

Introduction

The 1994 Uruguay Round Agreement on Agriculture (URAA) commits member countries of the World Trade Organization (WTO) to discipline their domestic agricultural support programs. Programs subject to annual spending limits are those that WTO members deemed, at the time, to have the greatest potential for stimulating too much production and thereby distorting world agricultural trade.

The goal of the Agreement is to “establish a fair and market-oriented agricultural trading system” through a series of reforms that, among other provisions, require WTO members to lower barriers to agricultural imports and to reduce their farm export subsidies. The URAA was unprecedented in that it was the first time (after seven previous trade rounds) that countries promised to make substantial changes in their domestic agricultural policies to facilitate more open trade.

At the same time, the UR commitments made by WTO members constrain their flexibility and spending choices when they consider ways to assist agricultural producers during economic downturns. For example, a WTO member cannot undertake or expand certain types of domestic farm programs that cause it to exceed an assigned annual spending limit for such programs.

As a WTO member and signer of the Agreement, these constraints affect the United States, which was a leading voice for agricultural trade reforms, including reductions in trade-distorting domestic subsidies. Since then, Congress, from 1998 through 2000, has passed a succession of bills appropriating a total of more than \$17 billion in *ad hoc* assistance to help agricultural producers cope with poor market conditions. The funds, along with billions of additional dollars in natural disaster aid, are over and above the aid already authorized for the sector under the 1996 omnibus farm law (P.L. 104-127). On June 26, 2001, the House passed a bill (H.R. 2213) providing another \$5.5 billion in *ad hoc* aid; Senate action was pending in mid-July.

Foreign competitors are closely monitoring U.S. actions. Some have raised concerns about this increased U.S. farm spending in light of the current WTO negotiations to further reform agricultural trade, which were initiated in March 2000.

Despite these high levels of support (relative to previous periods during the 1990s), the United States so far appears to be within its URAA prescribed annual spending limits. And, defenders of current U.S. farm policies point out that the 1994 Agreement, for example, has permitted the European Union (EU), a chief U.S. export competitor, to spend far more than the United States on domestic farm aid. They argue that so long as the EU and other foreign countries heavily subsidize their

farmers, a “free world market” in agriculture is illusory, and U.S. farm aid should not be singled out for criticism.¹

World trade obligations are a consideration as Congress debates the next major reauthorization of farm legislation. Most commodity price support provisions are due to expire by 2002, and a variety of potential farm policy changes already have been proposed.² Because of the interrelationships between trade and domestic support policies, lawmakers are interested in what the Agreement on Agriculture stipulates with regard to domestic supports, and how the various proposals might affect U.S. commitments under it.

Domestic Support Provisions of the Agreement³

Although the Agreement commits member countries to control their spending on domestic farm supports, it also permits them to exempt or exclude many types of programs. Broadly, the Agreement on Agriculture distinguishes between domestic policies that have the greatest potential to distort trade and therefore should be limited, and those that are less likely to distort trade. Negotiators (not the Agreement itself) used a color-code analogy for these categories, as described below.⁴

Amber Box Policies

Amber box policies are the most likely to cause producers to divert resources into or out of the production of various commodities, thus affecting supplies and world prices. Because of their potentially trade-distorting effects, these policies generally were subjected to gradually more stringent annual spending limitations under the Agreement.

¹ In late June 2000, U.S. officials offered a proposal at a WTO Agriculture Committee meeting that among other things would seek to reduce the differences in relative support between countries like the United States and the EU. For further discussion see page 14.

² See: *Farm Income and Commodity Price Support Proposals* in the CRS electronic briefing book on Agriculture Policy and Farm Bill; CRS Issue Brief IB10085, *The 2002 Farm Bill: Overview and Status*; CRS Report RL30847, *Agriculture: Previewing the 2002 Farm Bill*.

³ The Agreement on Agriculture was one of a series of agreements that came out of multilateral trade negotiations, which also created the World Trade Organization (WTO) as the institution to oversee world trade rules and referee disputes. As of April 2000, 136 countries were members. Sources for describing the Agreement are: U.S. Department of Agriculture, Economic Research Service (ERS), *Agriculture in the WTO* (WRS-98-4), December 1998; and *Message from the President Transmitting the Uruguay Round Trade Agreements, Texts of Agreements Implementing Bill, Statement of Administrative Action and Required Supporting Statements* (H. Doc. 103-316), September 27, 1994.

⁴ Part IV (Articles 6 and 7) of the Agreement on Agriculture contains the key provisions affecting countries' domestic support policies. (Export subsidies, considered to be distinct from domestic support subsidies, are covered in Article V of the Agreement.) For a step-by-step guide to these provisions, see CRS Report RS20840, *Farm Program Spending: What's Permitted Under the Uruguay Round Agreements*.

Examples of such policies or programs include price supports, where the government ensures that the farm price of a particular commodity will not fall beneath a prescribed level; direct payments tied to each unit of a commodity produced; subsidies on such inputs as fertilizer, seed, irrigation, or feed; and subsidized crop loans.

In the United States, programs that have been placed within the amber box include the dairy, peanut, and sugar price support programs; “marketing loan” programs for grains and cotton; crop storage payments; irrigation and grazing programs; and crop insurance programs.⁵

Each WTO member agreed that total annual spending for its amber box policies – termed a “Total Aggregate Measurement of Support” (AMS) – would not exceed a base period level (generally 1986-88). In addition, about 30 of these countries, including the United States and most other major agricultural traders, agreed to gradually reduce the maximum permitted levels of amber box spending each year, using the AMS calculation to determine this spending.

The developed countries agreed to reduce their total AMS by 20% from their base period, over a 6-year implementation period (1995-2000). Developing countries agreed to a 13% reduction over a 10-year period (1995-2004). Each member’s AMS for the final year of the implementation period is the “bound” level applying to each succeeding year after that – until a new trade agreement is negotiated. Any reductions do not have to be made equally across commodities or on a commodity-by-commodity basis. Each country can decide which programs to reduce, and how, in order to meet its obligation.

Annex 3 of the Agreement specifies the methods countries must use to calculate their AMS. For example, an AMS must be calculated on a product-specific basis for each agricultural product supported. Supports that are not product-specific (for example, irrigation subsidies) must be aggregated into one non-product specific AMS. National and sub-national (e.g., state) support must be counted; levies or fees on producers must be subtracted from the AMS calculation.

De Minimis Exclusion. Developed countries do not have to count amber box subsidies toward their total AMS if total support is equal to or less than 5% of the value of production (the exclusion is 10% for developing countries). Negotiators created this exclusion based on the theory that a subsidy is not likely to distort trade as long as it remains reasonably low. If subsidies apply to a specific product, e.g., wheat, sugar, etc., then the 5% rule applies to the value of production of that product. (All forms of non-exempt support for that product are totaled before the *de minimis* calculation is performed.) If subsidies are non-commodity specific, e.g., irrigation, then the 5% rule applies to the value of the country’s total agricultural production.

Country Commitments. Table 1 shows base period AMS commitments and final year (bound) commitments for the major agricultural traders. For developed

⁵ In late June 2001, the Administration reported that it was classifying \$2.8 billion in 1998 *ad hoc* assistance as amber; see page 18 for details.

countries the final year is 2000, and for developing countries (*in italics*) it is 2004. For example, the United States began from a base (1986-88) AMS of \$23.9 billion, and committed to not exceeding AMS levels of \$23.1 billion in 1995, \$22.3 billion in 1996, \$21.5 billion in 1997, \$20.7 billion in 1998, \$19.9 billion in 1999, and \$19.1 billion in 2000. In any year after that, its AMS cannot exceed \$19.1 billion.

Table 1. AMS Commitments, Selected Countries

Country	Base	2000	2004
<i>Argentina (million U.S. \$)</i>	87	80	75
Australia (million Aus. \$)	590	472	
<i>Brazil (million U.S. \$)</i>	1.1	1	0.9
Canada (million Can. \$)	5,376	4,301	
EU (million ECU)	80,975	67,159	
Japan (billion yen)	4,966	3,973	
<i>Korea (billion won)</i>	1,719	1,581	1,490
<i>Mexico (million Mex. \$)</i>	29,007	26,699	25,161
New Zealand (million N.Z. \$)	360	288	
Poland (million U.S. \$)	4,160	3,329	
South Africa (million rand)	2,519	2,015	
Switzerland-Lich.(million Sw.F)	5,321	4,257	
<i>Thailand (million baht)</i>	22,126	20,268	19,028
United States (million U.S. \$)	23,875	19,103	

SOURCE: World Trade Organization. AMS commitments do not count blue and green box subsidies, amber box spending beneath the 5% *de minimis*, and certain special and differential treatment of subsidies in developing countries.

Green Box Policies

Green box policies are those presumed to have the least potential for distorting production and trade and therefore are exempt from commitments to reduce or limit AMS spending. Annex 2 of the Agreement spells out in detail how to determine whether a domestic measure qualifies for the green box. Generally, support must be (1) provided through a publicly-funded program that does not involve transfers from consumers; and (2) not have the effect of providing price support to producers. In addition, specified programs can qualify for green box but only if they also conform to certain detailed “policy-specific” criteria, summarized as follows:

General services, including research; pest and disease control; training, extension and advisory services; inspection, marketing, and promotion services; construction of public infrastructure, all of which may qualify where they do not involve direct payments to producers or processors;

Public stockholding of commodities for food security, if it is an integral part of a food security program and stocks are acquired at current market prices;

Domestic food aid to needy persons subject to clearly defined criteria related to nutritional objectives;

Direct payments to agricultural producers of the following types:

- ! “Decoupled income support” not linked to the type or volume of commodity, and any condition of production after the base period, and not related to domestic or international prices after the base period;
- ! Income insurance and income safety net programs that relate solely to income (and not production or prices), within specified limits;
- ! Natural disaster assistance;
- ! Structural adjustment assistance that either involves removing land, livestock or other resources from agricultural production or through investment aids such as farm ownership and operating loans not tied to any type or volume of production;
- ! Payments for environmental or conservation purposes;
- ! Payments under regional assistance programs if limited to producers in a clearly delineated geographical area determined to be disadvantaged by “neutral and objective criteria.”

The most prominent example of a U.S. green box policy is the Production Flexibility Contract (PFC) payments being made under the Agricultural Market Transition Act (AMTA; Title I of the 1996 farm law). Under this law, those who formerly were enrolled in the annual USDA crop price and income support programs for grains and cotton, and who signed contracts, are receiving fixed but declining annual payments, totaling \$36 billion over the 7-year term of the law. The level of each recipient’s annual subsidy – known variously as a “Freedom to Farm,” “transition,” “PFC,” or “contract” payment – initially was determined by a farm’s past level of production of these particular crops, but this payment bears no relation to current production patterns. In other words, it is eligible to be placed in the green box because it is “decoupled,” U.S. officials have determined.

Other examples of U.S. green box policies include agricultural research and extension programs; the Conservation Reserve Program and the Environmental Quality Incentives Program; the food stamp and child nutrition programs (these domestic food programs account for a large share of U.S. green box spending); and meat, grain, and produce inspection, grading, and marketing activities.

Blue Box Policies

Blue box policies, also exempt from AMS calculations, include the following direct payments made under production-limiting programs: those based on fixed area and yield; those made on no more than 85% of base production; or payments tied to a fixed number of livestock (Article VI, paragraph 5). These criteria encompass the now-defunct U.S. target price deficiency payments made for grain and cotton prior to the 1996 farm law, and the EU's direct compensatory payments. The EU payments, linked to land use and to number livestock, were adopted with the 1992 Common Agricultural Policy (CAP) reforms to compensate farmers for significantly reduced market intervention prices. The blue box was created primarily to facilitate a compromise with the EU (until recently, the only major blue box user) so that the UR negotiations on agriculture could be brought to a successful conclusion.⁶

Countries' Performance to Date

Notification and Review

The Agreement on Agriculture requires countries to submit reports (notifications) on their implementation of the domestic support (as well as their export subsidy and market access) commitments, which in turn are reviewed periodically by the WTO Committee on Agriculture (Part XI, Article 18).

These notifications serve as the primary information source on what each country is spending on domestic agricultural policies, and on how they have chosen to classify these policies – i.e., what “color” they should be. The Agreement has provided member countries not only with some latitude in these determinations, but also in how quickly after each implementation year a notification is submitted. For example, as of mid-2001, numerous countries with reduction commitments had not yet submitted their 1999 or 2000 reports – including the United States. A few countries had not yet submitted their earlier years' notifications, either.

The U.S. notification for 1997 was not submitted until June 1999; the 1998 U.S. notification was not released until June 2001. The U.S. AMS is calculated on the basis of marketing years; that is, the 1998 implementation year began in 1998 and ended in 1999 for many commodities. (Countries may choose between the calendar, fiscal, or marketing year as their implementation year.) USDA analysts who prepare the notifications must wait until after the end of the marketing year when all spending and program details become available. Then more time typically is needed to review and calculate expenditures, and organize them into WTO formats and categories.

However, the 1998 U.S. notification was delayed for a longer period than usual due to officials' concern about the potential policy implications of how to classify the *ad hoc* farm payments – more specifically, the \$2.8 billion in so-called “market loss”

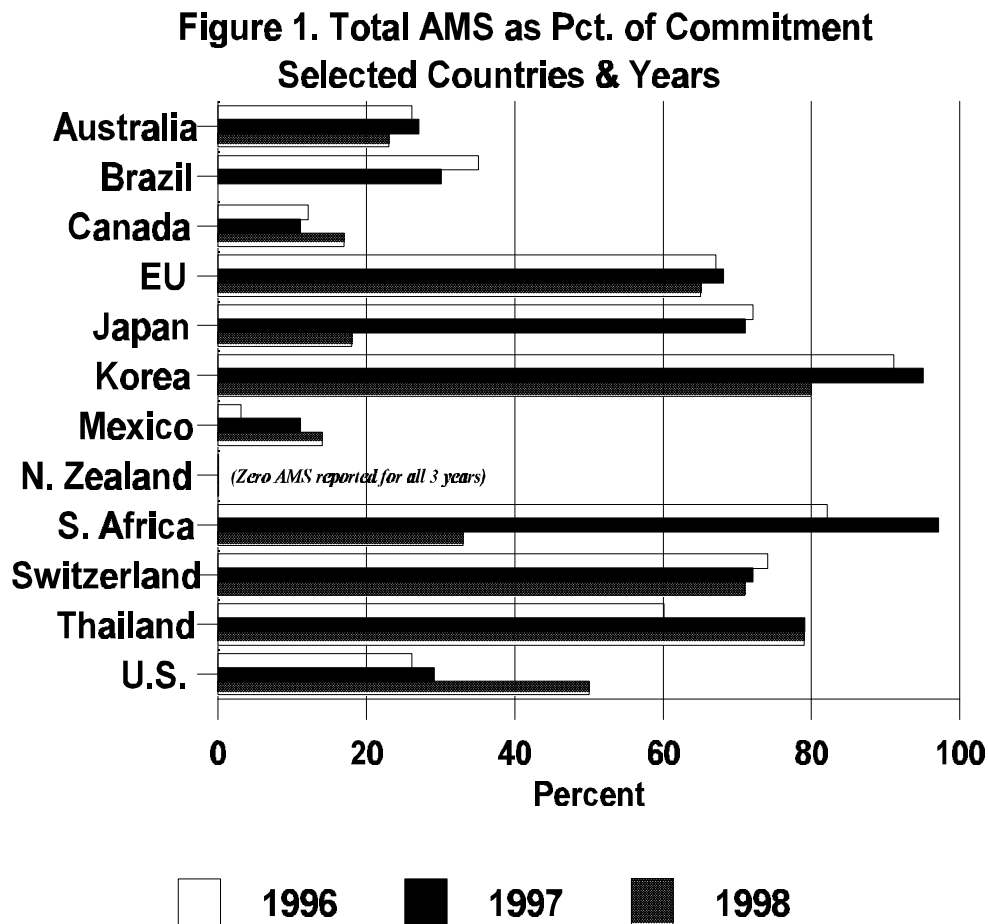
⁶ ERS, *Agriculture in the WTO*, page 15; and Young, Nelson, and Schnepf, “Domestic Farm Programs and the Upcoming WTO Negotiations,” *Choices* magazine, 3rd Quarter 1999. See also CRS Report RS20744, *Agricultural Support in the European Union and United States*.

payments made that year to those enrolled in the AMTA-PFC program. (See page 18 for details.)

AMS Notifications Compared

Nonetheless, in the latest notifications to the WTO, most countries reported that their AMS remained well below their commitments. Figure 1 shows selected major trading countries' reported total AMS for 1996 through 1999, expressed as a percentage of their annual commitments under the Agreement.⁷

Countries generally have been able to remain comfortably beneath their annual AMS commitments – at least through 1998 – for a number of reasons. First, major countries' spending on price-related support, an amber box subsidy, was relatively



high in 1986-88, the base period from which reductions are being made, due to low market prices during the base period. As world markets and farm prices strengthened in the 1990s, domestic support spending declined. Second, the United States, EU, and Japan have instituted policy changes that, they contend, have enabled them to

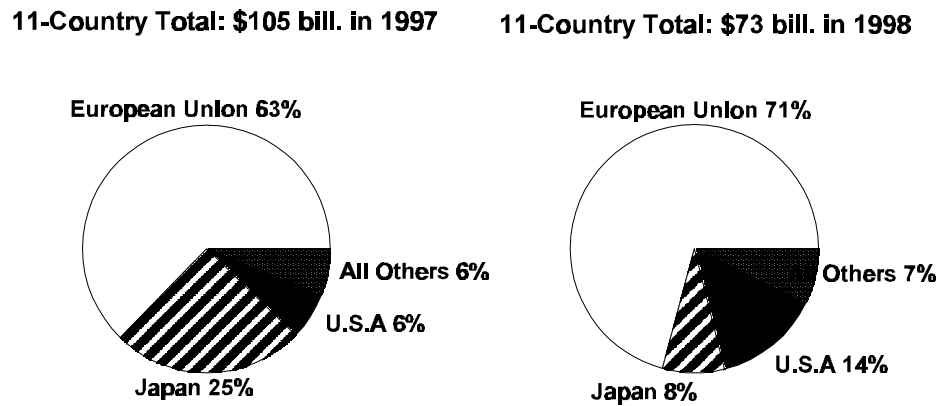
⁷ Source: WTO. As of mid-2001, Brazil had not made its notification for 1998. New Zealand reported zero AMS spending for all 3 years.

shift a significant part of their reported domestic support from the amber box to exempted methods, such as direct payments not tied to current prices.

Most if not all of the major trading countries are likely to claim compliance with AMS commitments in subsequent years' reports. However, analysts have observed that annual spending has been high in recent years. This is due in large part to the downturn in world agricultural markets in the late 1990s and the ensuing increase in the these countries' spending on amber box policies (also see "Farm Spending Trends" on page 10).

In 1997, the EU accounted for about \$66 billion, or 63%, of the total AMS reported by 11 leading agricultural trading countries. (as reported to the WTO and converted to U.S. dollars; see figure 2). Japan accounted for more than \$26 billion

Figure 2. Reported AMS, Selected Years

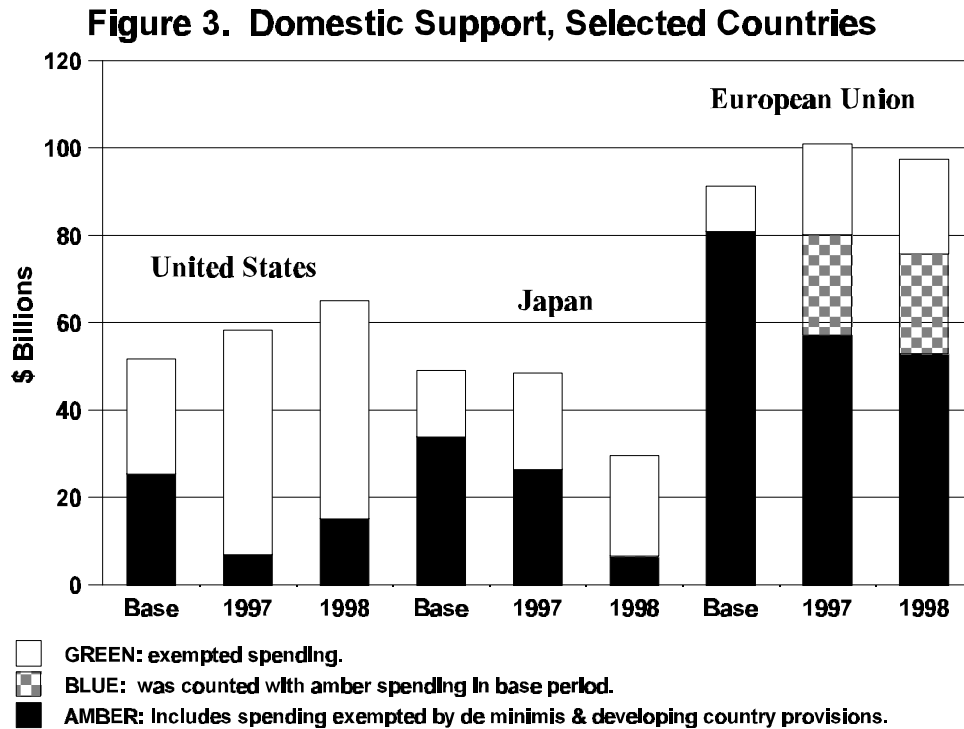


Countries: Australia, Canada, European Union, Japan, Korea, Mexico, New Zealand, South Africa, Switzerland, Thailand, United States.

or 25% of the total; the United States was a distant third with over \$6 billion or 6% in 1997. In 1998, the EU represented about \$51 billion or 71% of the 11-country total. The United States and Japan accounted for \$10 billion (14%), and \$6 billion (8%), respectively.⁸

⁸ CRS converted foreign currencies used in WTO notifications to U.S. dollars, using the average exchange rates for the year as reported by the International Monetary Fund (IMF) and, in some cases, by the WTO. Argentina and Brazil are major exporters, but had not submitted their notifications for 1998. (Argentina had not done so for 1997, either.)

Japan’s share decreased for 1998 primarily because it altered its support program for rice. Japanese officials assert that their rice policy is now exempt as a blue box policy because they have more closely linked rice payments to farm production limitations. Prior to that time, the Japanese reported their rice support as a costly and trade-distorting amber policy. (Critics point out that the Japanese rice regime remains highly trade-distorting because it relies on restrictive tariff rate quotas to protect the domestic industry.)⁹ Still, three countries represented over 90% of total reported AMS in 1997 and 1998.



SOURCE: WTO notifications. Local currencies converted to U.S. dollars based on average exchange rate for periods covered (using International Monetary Fund data).

Figure 3 indicates that, although amber box spending in these three countries has been below base period levels, spending which they have classified as green box increased substantially through 1998.

Selected Issues

The Uruguay Round provided new and strengthened rules for the conduct of agricultural trade. Continuing the process of agricultural trade liberalization has been a priority. Trade ministers of World Trade Organization (WTO) countries met

⁹ See: “Japan’s Changing Agricultural Policies,” in the April 2001 issue of USDA’s *Agricultural Outlook* magazine.

November 30-December 2, 1999, in Seattle, but were unable to agree on an agenda for a comprehensive new round of multilateral talks, which would have included not only agriculture, but many other, non-agricultural, issues. Another effort to launch a comprehensive round is expected when trade ministers meet again in November 2001 in Qatar.

However, because Article 20 of the URAA required that sectoral negotiations in agriculture begin in early 2000, these negotiations were launched March 23-24, 2000 at a special session of the WTO's Committee on Agriculture. Since then, countries have submitted their detailed negotiating proposals on agriculture (selected domestic support provisions of these proposals are discussed later in this section). The agricultural negotiations are under way, and proceeding slowly.

The "Peace Clause"

There is no deadline for concluding the agricultural negotiations. However, expiration, in 2003, of provisions under Article 13 of the URAA known as the "peace clause" could exert pressure on member countries to reach an agreement by then. Under provisions of the peace clause, as long as the subsidizing country is meeting its reduction commitments or other criteria agreed to in the UR, it is exempt from certain WTO challenges.

More specifically, WTO members, during the first 9 years of the URAA, must refrain from taking actions under domestic countervailing duty proceedings, or initiating WTO dispute settlement proceedings, alleging adverse effects or serious prejudice resulting from green box (permitted) subsidies. Members also cannot bring dispute settlement proceedings alleging nullification or impairment of UR tariff reductions that are the result of green box subsidies.

With regard to amber and blue box subsidies, WTO members are to exercise due restraint in initiating countervailing duty investigations. Amber box challenges may not be initiated so long as spending for a particular commodity does not exceed the level of its spending in the 1992 marketing year.

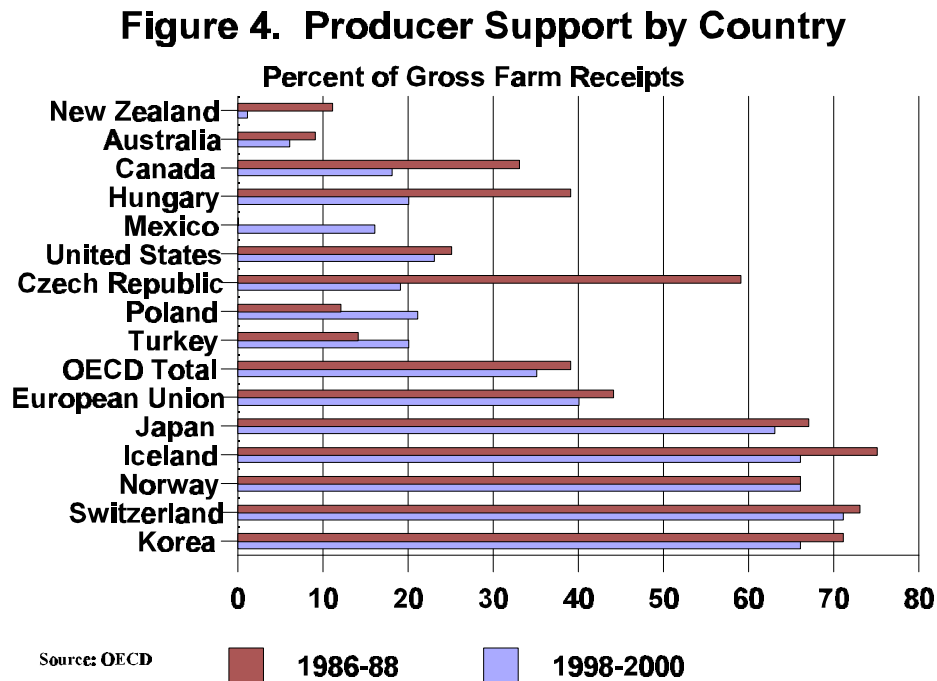
Some domestic agricultural interests have urged the United States to oppose any extension of the peace clause. They contend that the clause is preventing them from challenging the EU's blue box payments and seeking relief under WTO procedures. The EU has indicated that it wants to continue the peace clause.

Farm Spending Trends

Through 1997 and 1998, countries' annual AMS generally were below the levels to which they committed under the UR Agreement on Agriculture (and in most cases comfortably so). However, countries' overall domestic support remains high, when green box and other exempted spending (i.e., that which does not have to be counted as part of the AMS) is considered. Such overall domestic support – both exempt and nonexempt – is examined annually by the Organization for Economic Cooperation and Development (OECD) in its annual reports on domestic agricultural policies.

In its 2001 report, for example, OECD concluded that support to producers had decreased from 1999 to 2000, after rising the previous 2 years. OECD stated that the decline was a “positive development,” but “...like changes in previous years, reflected international price and exchange rate movements rather than major agricultural policy changes. There were no major policy reform initiatives and differences in the level of support among OECD countries widened.”¹⁰

In 1998-2000, total support to agriculture in the OECD countries was an estimated \$341 billion per year, on average, compared with an annual average of \$298 billion in 1986-1988 (nominal dollars). Estimated producer support as a percentage



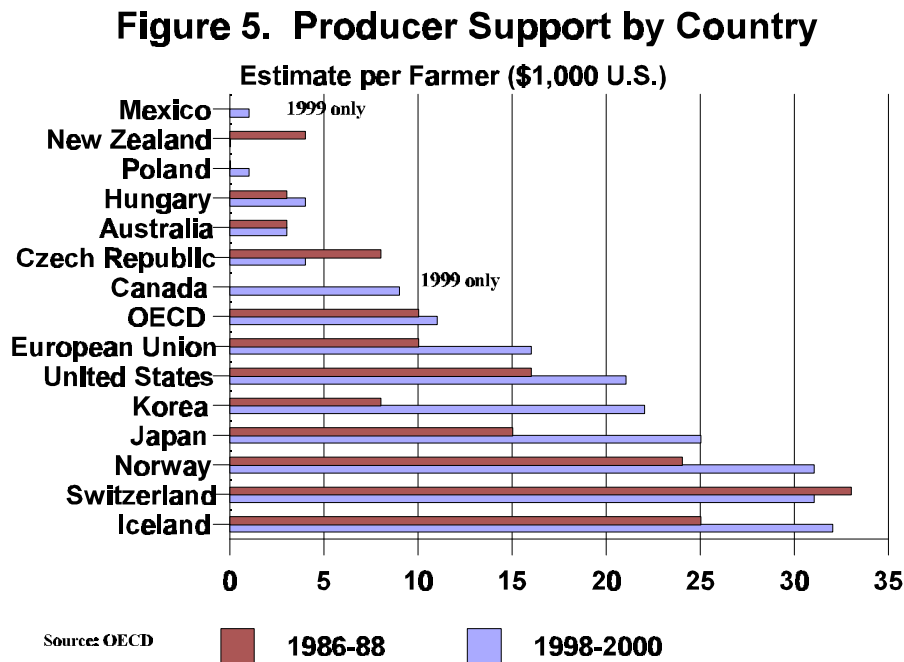
of total farm receipts for all OECD countries averaged 35% in 1998-2000 compared with 39% in 1986-88. (It decreased from 37% in 1999 to an estimated 34% in 2000.) Roughly four-fifths of the total in 1998-2000 went to individual producers, and the rest was for general services such as infrastructure, research, and marketing. Market price support (where consumers generally pay higher prices to ensure farmers receive higher incomes) and output payments accounted for most producer support.¹¹

¹⁰ OECD. *Agricultural Policies in OECD Countries: Monitoring and Evaluation, 2001*. OECD was established to promote economic growth, higher living standards, and trade expansion worldwide. OECD Members are Australia, Austria, Belgium, Canada, the Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Japan, Korea, Luxembourg, Mexico, the Netherlands, New Zealand, Norway, Poland, Portugal, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States.

¹¹ The OECD data differ from that collected by the WTO for AMS reporting purposes, and (continued...)

These forms of support “are among the most production and trade-distorting,” OECD observed. The 2001 report also documented the wide differences in support provided among countries in 1998-2000, from 6% and 1% of farm receipts in Australia and New Zealand, respectively, to about 65% or more in Iceland, Japan, Korea, Norway, and Switzerland (figure 4). Sugar, milk, and rice received particularly high levels of support.

The following countries spent, on average, more than \$20,000 per full-time farmer in 1998-2000: Iceland, Switzerland, Norway, Japan, Korea, and the United States (figure 5).



Effectiveness of Current Agreement on Agriculture

OECD's 2000 report on agricultural subsidies stated:

The upward movement in support to agriculture, first evident in 1998, continued in 1999, with support reaching the high levels of a decade earlier. Low world commodity prices, and the resulting pressure they put on farm incomes, led many OECD countries to introduce new measures or to provide additional support to farmers. The ways in which these measures were implemented were, in many

¹¹ (...continued)

therefore are not directly comparable. For example, if the OECD support were categorized as was done for WTO, some would fall in the amber box and some would be exempt. Also, the OECD counts more forms of government intervention than just the internal measures used for the WTO calculations of AMS.

*cases, inconsistent with the longer-term principles of agricultural policy reform.*¹²

In its 2001 report, OECD noted:

*Despite some shift away from market price support and output payments, these continue to be the dominant forms of support in most countries, insulating farmers from world market signals and distorting global production and trade...Overall, progress towards further policy reform agreed to by OECD Ministers has been insufficient and remains fragile.*¹³

Some analysts contend that the relatively high levels in domestic agricultural subsidies documented by OECD – which, they believe, likely will also be reflected in countries’ future AMS notifications – can be attributed at least partly to language of the UR Agreement, which, in their view, has not been effective in curbing spending. First, the Agreement set high base levels from which countries are making their annual reductions. The United States, the EU, and other leading agricultural traders were able to claim credit for spending cuts they already had made before the Agreement took effect in 1994.

Second, various exemptions in the URAA have shielded some large subsidies from any required cutbacks at all, they add, citing the creation of the blue box that protects the EU’s compensatory payments. On the other hand, starting from a higher base, and creating the blue box category, was viewed by many as the only way to conclude a deal and at least begin the long process toward meaningful reforms.

Third, the categorization and reporting of subsidies are largely self-policing, these analysts point out. That is, each member country has considerable discretion in determining whether a subsidy is “green” or “amber” and, if it is the latter, in calculating its value for WTO reporting purposes. Such discretion makes countries’ choices subject to criticism and future challenges by other WTO members, according to USDA and other analysts. Defenders of the URAA language contend that it is sufficiently explicit to prevent WTO members from undermining the basic objectives of the URAA.

Fourth, green box expenditures for many countries appear to be increasing. Such expenditures – including direct payments to farmers so long as they are not tied to prices and production – were presumed by UR negotiators to have the least likely effect on trade. “However, any policy that transfers income to producers could conceivably have some effect on production by increasing wealth and reducing the risk of financial failure. Some specific policies that otherwise might meet the URAA green box criteria could have significant positive effects on production if financed with a large enough total amount of government expenditure.”¹⁴

¹² OECD. *Agricultural Policies in OECD Countries: Monitoring and Evaluation, 2000.*

¹³ OECD. *Agricultural Policies in OECD Countries: Monitoring and Evaluation, 2001.*

¹⁴ ERS. *Agriculture in the WTO*, page 19.

In another recent report, OECD confirmed that green box and other exempt policies have assumed greater importance, observing that over 60% of domestic agricultural support in OECD countries is excluded from WTO reduction commitments. Many of these exempt policies, although they may be less trade distorting than traditional market price support, still have production and trade effects. The OECD report called for more research on whether green box payments really are minimally trade distorting, which could “contribute to the further development of more rigorous operational criteria for exemption from reduction commitments.”¹⁵

For example, the U.S. Congress has provided \$25 billion in *ad hoc* assistance provided to U.S. producers between 1998 and 2000 (\$17 billion of it to address poor market conditions and most of the rest for disaster assistance), and another \$5.5 billion or more is expected to be provided for 2001. While much of this aid is expected to be exempted from AMS calculations, the OECD reports that its provision for 3 consecutive years “...gives a strong signal to farmers that they can expect to receive extra support at times of low world prices and may, as a result, contribute to world price depression.”¹⁶ (See “Implications for U.S. Agricultural Policy,” below, for a more detailed discussion.)

The EU’s exempted blue box payments (based on fixed area and yields or a fixed number of livestock) are no less contentious. These payments, which have been \$23-\$24 billion annually, are considered by many analysts to be trade-distorting. “Payments for exempt blue box policies compensate producers for foregone income. Blue box payments received in excess of foregone income from program compliance immediately increase producer wealth, lead to expectations of future windfalls, and may encourage expanded production, especially if any production limitations are subsequently relaxed,” USDA observed.¹⁷

Future Reforms in Domestic Supports

WTO members bring to the new negotiating round a divergence of viewpoints on how to handle domestic farm supports. These range from countries that will seek continuing and deeper reductions in spending, to those that are likely to defend their internal subsidies as necessary for various national policy reasons.

In the United States, agricultural interests have long complained that the EU and Japan were permitted, under the URAA, to begin their AMS reductions from base spending that was much higher than the U.S. base level. Moreover, the Japanese bound (allowable) AMS level at the end of implementation (2000) will be approximately twice the U.S. level, at \$37.1 billion versus \$19.1 billion. The EU’s

¹⁵ OECD. *The Uruguay Round Agreement on Agriculture: An Evaluation of its Implementation in OECD Countries*. 2001.

¹⁶ OECD. *Agricultural Policies in OECD Countries: Monitoring and Evaluation, 2001*.

¹⁷ ERS. *Agriculture in the WTO*, page 18. The OECD also has asserted that increased output-based payments generally (along with price supports) contribute to lower world prices and impose costs on producers in countries that do not protect their domestic markets.

final bound level is likely to be more than \$60 billion when converted from EU to U.S. currency, or more than three times the U.S. level. Moreover, if the estimated \$24-\$25 billion or more in EU blue box payments were included, EU spending might be more than 4 times the U.S. bound level.

U.S. Proposal. Concerns about this large disparity in spending undergird the U.S. proposal for achieving further reductions in domestic and export subsidies and in agricultural trade barriers, which was presented to the WTO Agriculture Committee in June 2000. The proposal includes the following key elements:

- Domestic support disciplines would be “simplified” by placing supports in one of two (rather than the current three) categories: exempt supports, for those with no, or minimally, distorting effects on production or trade; and nonexempt supports subject to reduction commitments. This effectively would eliminate the blue box exemption claimed by the EU for its compensatory payments.
- Nonexempt supports would be reduced as follows: reductions would start at member countries’ final bound AMS; each one’s AMS would be reduced to a new final bound level that is equal to a fixed percentage of the members’ value of total agricultural production; this fixed percentage would be the same for all members – for example, 10%, 15%, or some other figure yet to be negotiated; and reductions would be made through progressive annual reductions over a fixed period. In summary, while final levels of support (in absolute value) might still differ among countries, they would be the same when measured as a proportion of the country’s production value.
- The criteria for determining exempted support measures would be “enhanced further...while ensuring all exempt measures are targeted, transparent, and, at most, minimally trade distorting.”
- Special consideration would be given for exemptions of support measures that are essential to the development objectives of developing countries.

EU Proposal. EU officials have criticized the U.S. proposal, arguing that its formula would require few if any cuts in U.S. farm programs, because U.S. support as a percentage of the value of total output is much lower than the EU’s (see figure 4). If reduction formulas were based on support per farmer, the United States would be required to make larger reductions (see figure 5).¹⁸

The EU tabled its own comprehensive proposal for reforming agricultural trade in December 2000.¹⁹ Key elements affecting domestic subsidies include:

- The need to recognize the “multifunctional role of agriculture” (see “Multifunctionality” and Nontrade Objectives, on page 17, for an explanation);

¹⁸ “U.S. Agriculture Proposal Receives Mixed Response at WTO Talks,” *Inside U.S. Trade*, July 7, 2000.

¹⁹ *EC Comprehensive Negotiating Proposal (G/AG/NG/W/90)*, December 14, 2000.

- Acknowledgment that the current URAA framework for addressing domestic supports generally is appropriate, providing a basis for aid that moves away from price support towards more transparent and less trade distorting policies. Aid which varies in relation to market price changes can be particularly trade distorting and should specifically be disciplined;
- Pursuit of further AMS reductions, starting from final bound commitment levels under the 1994 agreement, “by a further strengthening of the rules concerning non-product specific domestic support, and a by a reduction of the ‘de minimis’ clause for developed countries;”
- Retention of the concept of the blue and green boxes and the general rules for their use, although detailed rules would be open for discussion;
- A re-examination of the criteria for placing measures into the green box to ensure both minimal trade distortion and at the same time appropriate coverage of other societal goals such as environmental protection and rural development (see “Multifunctionality” and Nontrade Objectives, page 17);
- Specific disciplines applied to variable amber box subsidies that effectively increase exports by providing compensation for market price variations.

Defending its blue box payments in a paper submitted to the WTO Committee on Agriculture in June 2000, the EU cited an OECD simulation analysis that found: “...compared to market support, area payments in one country or region, whether tied to a requirement to plant or not, lead to smaller production, trade and welfare impacts on other countries and regions.”²⁰

Cairns Group Proposal. The Cairns group of agricultural exporting countries submitted its proposal on domestic support in September 2000. The group declared that current disciplines and reductions are “clearly inadequate and have not resulted in a fundamental shift away from trade and production-distorting forms of domestic support.”²¹ More specifically, the proposal includes:

- Use of a formula approach to achieve “major reductions in trade and production distorting domestic support, including AMS and blue box, leading to the elimination of such support and thus the removal of disparities in the levels of

²⁰ OECD, *A Matrix Approach to Evaluating Policy: Preliminary Findings from the Policy Evaluation Matrix Pilot Studies of Crop Policy in the EU, the U.S. Canada, and Mexico*, February 2000, as quoted in WTO, *European Communities Proposal: The Blue Box and Other Support Measures to Agriculture* (G/AG/NG/W/17), June 28, 2000.

²¹ *Cairns Group Negotiating Proposal, Domestic Support* (G/AG/NG/W/35), September 22, 2000. The Cairns group (formed in 1986 in Cairns, Australia) includes Argentina, Australia, Brazil, Canada, Chile, Colombia, Fiji, Indonesia, Malaysia, New Zealand, Paraguay, the Philippines, South Africa, Thailand, and Uruguay. The group has been the most vocal in calling for the removal of trade barriers and for substantial reductions in subsidies affecting trade.

this support...” with the time period and other parameters agreed to in the negotiations;

- A “substantial downpayment” in the first year of implementation – e.g., not less than a 50% initial reduction in trade and production-distorting supports;
- Commitments that are “disaggregated” to ensure that the reductions will occur on all agricultural products (for an explanation, see Other Issues, on page 17);
- Review of green box criteria to ensure that all such supports fundamentally are not, or are no more than minimally, trade- or production-distorting;
- Recognition of the need for special and differential treatment to assist developing countries.

Developing Countries’ Views. A June 2000 submission to the WTO by a group of 11 developing countries focuses on the concept of special and differential treatment for such countries, which generally infers greater flexibility and longer phase-in periods for WTO rules. The submission criticizes the developed countries for increasing domestic subsidies (including those in the green box). The developing countries’ proposal recommends the creation of a “Development Box” with policy measures that aim to enhance developing countries’ food security and their capacity to produce their own food; to sustain employment for the rural poor; to support small farmers; and for other purposes (see also “Multifunctionality” and Non-trade Objectives,” on the following page). They also argue for eliminating the green box category in favor of a single general box for all subsidies, with a fixed common level of support, above which subsidies would be prohibited.

“Multifunctionality” and Non-trade Objectives. The EU, along with Japan and several other countries, have voiced concern that reforms in agricultural trade should not come at the expense of other policy objectives important to an individual country. They have introduced a widely discussed concept commonly known as “multifunctionality of agriculture.” Proponents of this concept argue that production-linked support for agriculture may be necessary to achieve socially desirable benefits that are not necessarily agricultural. They believe that exemptions should be permitted if such support creates such benefits as open space, biodiversity, food safety, protection of soil and water resources; contributes to cultural goals; alleviates poverty; and/or sustains the economic viability of rural communities. The United States generally has argued that trade-distorting measures and protection should not be used to pursue non-trade objectives. The United States and Cairns Group view multifunctionality and food security as disguised rationales for shielding agriculture through the use of trade-distorting support and protection.²²

Other nontrade objectives also could be introduced into the negotiations. For example, the EU has cited its growing body of legislation on animal protection, covering farming, transport, slaughter and experimentation. It noted, in a June 2000

²² See also USDA/ERS, *Multifunctionality in the WTO trade negotiations (overview)*, at: [<http://www.ers.usda.gov/briefing/WTO/multifunctionalityoverview.htm>].

submission to the WTO, that “high animal welfare standards can increase costs to producers over and above any possible increased returns from the market,” and that “trade liberalization can exacerbate this effect.”²³ In its December 2000 comprehensive submission, the EU proposes, as possible actions to address animal welfare, the development of multilateral agreements, appropriate labeling, and exempting “compensation of additional costs to meet animal welfare standards from reduction commitments where it can be clearly shown that these costs stem directly from the adoption of higher standards...”

Another nontrade objective is food security, which some countries define as the ability for their own producers to provide all, or at least much, of the food needs of the population. On food security, Japan has stated that domestic agricultural production should have the primary role of ensuring food supply by increasing production, and it consequently calls for an examination of policy interventions in support of that role. Others including the United States embrace a broader definition of food security whereby people have the means to obtain adequate food either by growing it themselves or by earning enough income to buy it at home or overseas.

Other Issues. Currently, commitments to reduce domestic subsidies are on an aggregated basis – that is, support for individual commodities are combined into a total annual level of spending for the purposes of reporting AMS. Under this approach, countries can seek competitive advantage in one commodity area and reduce subsidies in another. Some suggest that commitments be “disaggregated” so that future limitations on support would be commodity-specific, particularly for those commodities that are more heavily subsidized such as dairy, sugar, and various grains. Other considerations include the relationship between reforms in domestic support and other trade policies (i.e., export subsidies and import barriers); whether reduction commitments, which are now expressed in nominal terms, should be adjusted to account for inflation and currency exchange rates; and the production and trade effects of the current 5% *de minimis* rule.²⁴

Implications for U.S. Agricultural Policy

The URAA potentially imposes constraints on U.S. policymakers in considering both short-term economic relief for farmers and longer term policy. Most provisions of the 1996 farm law (P.L. 104-127) expire in 2002. Congress already is considering legislation to succeed the 1996 law. The House Agriculture Committee, for example, was expected to begin markup in late July 2001; the Senate Agriculture Committee has been holding hearings on a new bill.

²³ WTO, *European Communities Proposal: Animal Welfare and Trade in Agriculture* (G/AG/NG/W/19), June 28, 2000.

²⁴ For more information see the ERS briefing room on the World Trade Organization at: [<http://www.ers.usda.gov/briefing/WTO/>], and *Agriculture: Work in the WTO, The Current Negotiations*, at the WTO site: [http://www.wto.org/english/tratop_e/agric_e/negoti_e.htm].

The key section of the 1996 law, Title I (AMTA), was intended to accelerate an ongoing policy trend toward exposing U.S. farmers to the greater opportunities, but also the higher risks, of the global marketplace. This was done primarily by ending the payments made to grain and cotton producers that were tied to production and prices, and replacing them with gradually declining “transition” payments, totaling about \$36 billion over the 7 years ending in 2002.

However, the fact that billions of dollars in supplemental payments have been provided by Congress for 3 years in a row (and are likely to be provided again in 2001), in response to the downturn in prices for major farm commodities, has caused a closer and critical examination of the 1996 policy direction. When these supplemental payments are added to already programmed spending, outlays for U.S. commodity programs are reaching record levels, despite a policy that initially was intended to wean farmers from federal support.²⁵

Ad Hoc Relief

There was intense interest, here and abroad, in how the United States would classify, for its WTO notifications, the *ad hoc* farm assistance. The 1998 AMS notification, made in June 2001, was the first to reflect this assistance. In this notification, the \$2.8 billion in market loss payments to PFC participants ultimately were classified as amber (i.e., potentially trade-distorting), but not counted toward the AMS because they were determined to be non-commodity specific support, and their cost was not high enough to make all non-commodity specific spending for the year exceed the 5% *de minimis* threshold. In other words, when the payments were added to all other non-product-specific support, the total (\$4.6 billion) was still beneath the *de minimis* threshold of 5% of the value of all U.S. agricultural production. (This value was \$191 billion in 1998; 5% of this figure is about \$9.5 billion).

The decision to classify the payments as amber was controversial – even though they did not have to be counted toward the AMS for 1998. “Under WTO rules, these market loss payments must be classified in the amber box,” the Secretary of Agriculture announced in June. “By classifying them properly, we set the right precedent for other nations in the way they classify their own trade-distorting subsidies, and we set an open and above-board tone as we move toward a challenging new round of trade negotiations in the WTO.” Some agricultural interests supported the decision; the American Farm Bureau Federation (AFBF), for example, noted that the market loss payments were made in response to low farm prices, and that classifying them as amber maintained the credibility of the system.²⁶

Others, including the House Agriculture Committee Chairman, criticized the Administration for classifying the payments as amber. The chairman argued that the

²⁵ Net outlays for crop loan-related subsidies alone have increased from zero in FY1996 and FY1997 to \$8.1 billion in FY2000 and an estimated \$6.4 billion in FY2001. Such subsidies are authorized by the 1996 farm law, but the high level of outlays, a result of low market prices, was not anticipated at the time. These types of loan-related outlays are counted toward the AMS in U.S. notifications to the WTO.

²⁶ Statement by Bob Stallman, AFBF President, June 22, 2001.

payments should have been placed in the green box because they were provided after the production year and thus could not influence planting decisions. "The USDA decision creates a precedent for classifying assistance that will apply to payments also made in 1999 and 2000, as well as restrict our ability to make these payments in the future," the chairman stated, adding: "Since market loss payments are based on Agricultural Market Transition Act payments, this action could call into question the placement of non-trade distorting AMTA payments in the WTO green box."²⁷

Long Term Farm Policy

The next omnibus farm bill is expected to be signed into law before the WTO negotiations on agriculture are concluded. The long-term farm policy developed in this measure is likely to be shaped not only by current U.S. and world market conditions and by federal budgetary constraints (as they almost always do), but also by WTO developments. More specifically, congressional perceptions of progress in agricultural trade reform, and of other countries' (e.g., the EU's) commitments to further discipline their own domestic farm spending also could influence the type and level of assistance that U.S. farmers may be provided after 2002.

At the same time, the official U.S. negotiating position in the WTO is to continue to further reduce trade-distorting domestic farm subsidies and to achieve a more equitable balance among member nations. Thus, lawmakers are paying close attention to how various policy options might affect both current U.S. URAA obligations, and U.S. negotiations in the new round.

Lawmakers have been asking which "box" – amber or green – the farm support proposals, now being offered by agricultural interest groups, might belong. Those perceived to have the least potential to distort trade, and to be exempt from WTO reduction commitments, might ultimately be viewed as the most attractive, particularly if they also achieve other key policy goals, most notably raising farm income. Examples of such proposals include direct payments not linked to production or prices, assistance to achieve environmental and conservation goals on the farm, and funding for research and market development.

One policy option receiving widespread attention and support is some form of new "counter-cyclical assistance" – generally as a supplement to other, existing policy tools such as marketing loans and fixed payments. Although the various counter-cyclical proposals differ in detail, they all share a common objective: to build into standing law an automatic trigger that would provide more government support when farm prices and/or incomes decline, and less support when they improve.²⁸

However, the URAA requires that programs tied to current prices or production be counted as amber. Some groups have argued that their counter-cyclical proposals

²⁷ House Agriculture Committee press release, June 22, 2001.

²⁸ For an explanation of this policy approach, see [What Is "Counter-Cyclical Assistance"?](#) In the CRS electronic briefing book on Agricultural Policy and the Farm Bill, and CRS Report RS20901, *Farm "Counter-Cyclical Assistance."*

could be designed in a way that they would not be amber (i.e., trade-distorting). For example, if payments to farmers were triggered by low income (as measured by gross receipts for one or more commodities) rather than low prices, they would be exempt, they argue. Others disagree, noting that it is usually low prices that cause low income. The current Under Secretary of Agriculture for Farm and Foreign Agriculture stated in June 2001 that he has not yet found a counter-cyclical proposal that would satisfy the WTO green box definition.

The counter-cyclical approach is just one of several major options now being debated for inclusion in a new farm bill. It is not yet clear what types of program tools Congress ultimately will choose for supporting domestic agriculture in 2002 and beyond. But most observers believe that trade considerations will be a significant consideration in their development.