

# Disciplines on Agri-Food Trade: Toward a Renewed Framework



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## The Issue

Trade is very near the top of the Canadian agri-food policy agenda. In just over two years, Canada has engaged three major trade agreements- the Comprehensive Economic and Trade Agreement (CETA) with the EU- expected to be ratified soon, the Trans-Pacific Partnership (TPP) with consultations on Canada's ratification ongoing, and the WTO-Nairobi Agreement on export competition which may effectively conclude the Doha Round.

But while trade is at the forefront of agri-food policy discussions, as it must be for a trading nation like Canada, it is hardly a subject of consensus. There are some who feel that freer trade generates structurally unfair outcomes, apparently motivated by concerns of social justice and allocation of benefits from trade. Others worry that in some ways trade is slanted in favour of certain countries and that a non-level playing field is endemic to global agri-food trade, or that trade agreements somehow seem to never live up to their billing. These views clash with those of others who focus on the overwhelming interest of Canada in liberalized trade in farm and food products, regardless of whether trade agreements really achieve as much as they could or should.

The WTO Agreement on Agriculture came into effect over 20 years ago. The basic premise in the agreement was that three comprehensive areas needed greater discipline: market access, domestic support, and export competition (the three "pillars"). The premise was based on a large body of research conducted in the 1980s and early 1990s to both understand the policies and programs countries were employing, and to identify qualitatively and quantitatively their impact on trade flows and competition among exporters and importers. Since that time, trade in food and agriculture has changed considerably.

In this note, we briefly examine whether these disciplines have lived up to their promise in the agreement. We argue that while important gains have been made in disciplining trade distortions, other measures have been introduced that lie outside of the three pillars identified in the WTO, weakening the move to a more liberal trading environment for agriculture and food. Equally, the way in which countries have notified policies and programs affecting trade needs greater exploration; that is, are member countries living up to the ambitions and expectations of the 1994 Agreement? Finally, we argue that a more comprehensive framework that goes beyond the original three pillars needs to be designed, supported by a significant research effort, to capture the impacts on trade and trade flows in a substantially changed world for food and agriculture.

## Current State of Play

The Uruguay Round results held the promise of reductions in domestic support for agriculture through the measurement, limitations, and reporting of domestic support by all members. The Doha Round negotiations enunciated an intent to extend these commitments for further reductions in domestic support. The Uruguay Round Agreement defined limits on some domestic support using the Aggregate Measurement of Support (AMS). For the Doha Round, a more complex set of limits has been proposed, although still based on direct and indirect government support as well as market price support.<sup>1</sup> The issue is whether these limits have been effective in reducing domestic support across member countries and reducing the trade distortions arising from such subsidies.

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<sup>1</sup> For details of the AMS and the proposed limits for the Doha Round, see: Lars Brink, 2015. Policy Space in Agriculture under the WTO Rules on Domestic Support. IATRC Working Papers. Accessed at: <http://purl.umn.edu/207090>

Additionally, agricultural trade relationships have changed dramatically since the Uruguay Round was concluded, with several developing countries sharply increasing domestic support levels, and participating to a considerably greater extent in agricultural trade.

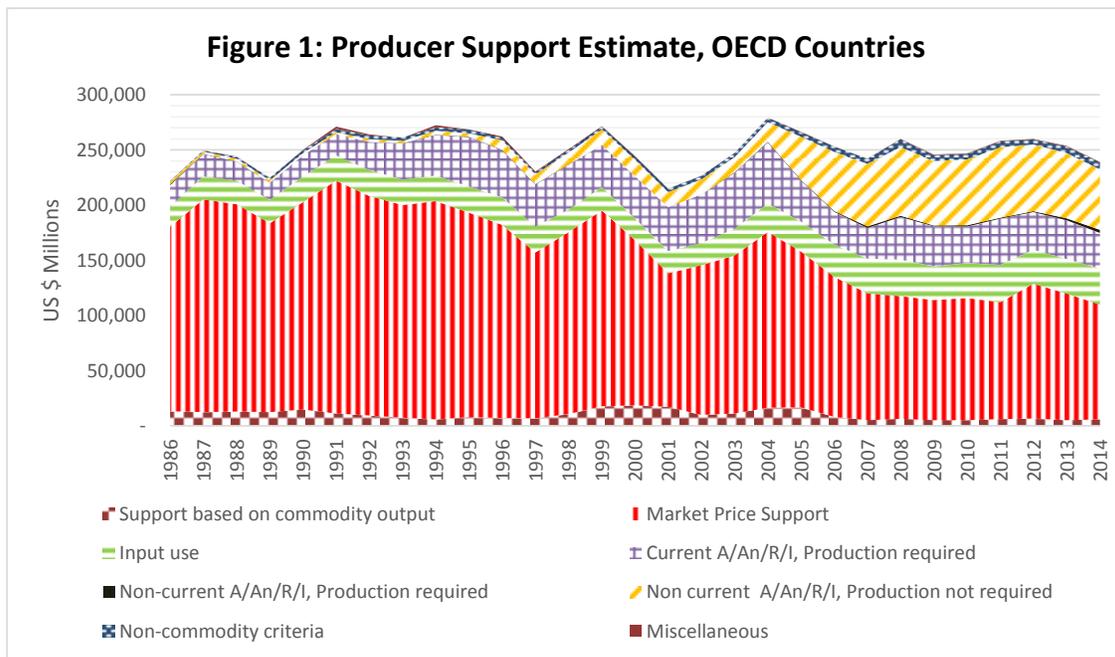
Figure 1 presents an illustration. It plots the major elements of agricultural support used in the calculation of the Producer Support Estimate for OECD countries since 1986, in nominal terms. It shows that estimated total producer support for OECD countries in 2014 was just under \$US 240 billion. This is not that much different than in late 1980's and throughout the Uruguay Round negotiations.

What has changed materially are the forms of support provided. The forms of support traditionally viewed as most distorting and captured in the AMS measure—market price support, payments based on output, subsidies on input use, and payments based on output history requiring current production have either declined (most notably market price support and payments on

output) or remained about the same. Since 1995 some countries have changed policy such that their payments qualify for exemption from the AMS.

Alternative forms of support exempted from the AMS have either remained about constant or increased. In particular, support to farmers based upon historical output but not requiring current production<sup>2</sup> has increased greatly, approximately in proportion to decreases in market price support and support based on outputs. So while the data are not inflation adjusted, it is hard to argue that overall support to agriculture has really come down materially. There has been a shift in who provides support, which results from increases in some countries offsetting the declines in other countries

Moreover, the OECD reports that “In most of the emerging economies, however, the monetary value of total agricultural support has been increasing over time. The increase was particularly rapid in Indonesia, the Russian Federation, Brazil, Kazakhstan, and China where the average annual real growth rates of the TSE (total



<sup>2</sup> Especially payments based on historical production in which current production is not required. A/An/R/I means A (area planted) / An (animal numbers) / R (receipts) / I (income)

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support estimate) over the 1995-97 to 2012-14 period were 43%, 33%, 26%, 25%, and 22% respectively<sup>3</sup>. Another example would be India, where much of its support to agriculture is provided through input subsidies for low-income or resource-poor farmers claimed as exempt from the AMSs<sup>4</sup> and thus without constraint under the WTO. In its 2016 National Trade Estimate Report, the Office of the United States Trade Representative identifies agricultural support in India and China as a trade irritant for the US<sup>5</sup>.

### How We Got Here

In agri-food trade discussions, there exists a common lingo, or format that describes the critical nature and aspects of agri-food trade. This format, or “pillars”-domestic support, export competition, and market access- is also used to define the disciplines placed on agri-food trade policy. For many, these are taken for granted as the intrinsic or obvious elements of trade policy. In fact, this common framework had to be developed, mostly in the 1980's, and became codified in the Uruguay Round Agreement on Agriculture, along with the criteria-based based exemptions of some policy measures from the domestic support limits.

As the Tokyo Round of trade negotiations under the General Agreement on Tariffs and Trade (GATT) was winding down in the late 1970's, agriculture was dropped from serious consideration because there was no possibility of bridging the differences in views among the major players with respect to trade disciplines. But the failure identified a significant problem in the way in which the agricultural trade negotiations had taken place. The focus of negotiations through the Tokyo Round was on highly specific issues, often bilateral, and undertaken almost entirely as bids and offers between countries and extended to other countries through preferential arrangements. There was no particular framework for systematic disciplines on governmental policies and

programs that affected agri-food trade relationships within which the negotiations were pursued. In addition, the negotiations were undertaken primarily among developed countries, and largely ignored the growing importance and concerns of developing nations.

After the Tokyo Round, it was recognized that many more nations would need to be involved in future agricultural trade negotiations. By 1984, many developing nations had agreed to join the GATT, rather than create their own trade arrangements, separate from the GATT through the United Nations Conference on Trade and Development (UNCTAD). A majority of members agreed to start negotiations by 1986. But they also made clear that the issues in agriculture raised by developing nation members had to be resolved if agreement was to be achieved. This was a considerable departure from previous rounds, where agriculture was the problem child that was often set aside to achieve the overall agreement.

The failure of the Tokyo Round spurred a number of groups to start designing a framework for subsequent negotiations, to focus on the broad problems across agricultural trade liberalization rather than specific bilateral issues among members. Part of this work also stemmed from the development of the Producer Subsidy Equivalent (PSE), created in the early 1970s, to measure the extent of domestic and border measures and intervention in agriculture as a whole and for specific commodities. It offered a comparative measure of protection across countries. Other concepts were also explored including nominal and real rates of protection, and assessments of various types of subsidies and market price support affecting agricultural trade. Over time, it led toward the development of the framework for the Uruguay Round's three pillars in agriculture: domestic subsidies, tariff and non-tariff barriers (access), and export subsidies. These issues focused attention on the multilateral aspects of trade liberalization rather than solely on the bilateral bids and offers between members. The PSE was the analytical basis for the negotiated definition of the AMS in the Uruguay Round, even though it was certainly not as robust or comprehensive as the earlier versions of PSEs. Without such a framework, the rules for exempting policies (green box, blue box,

<sup>3</sup> OECD, 2015. Agricultural Policy Monitoring and Evaluation 2015. p 34. DOI: [10.1787/agr\\_pol-2015-en](https://doi.org/10.1787/agr_pol-2015-en).

<sup>4</sup> Under Article 6.2, WTO Agreement on Agriculture.

<sup>5</sup> <https://ustr.gov/sites/default/files/2016-NTE-Report-FINAL.pdf>

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input subsidies in developing countries) and measuring support, and the limits on certain support, the Uruguay Round would have faced the risk of an outcome similar to that of the Tokyo Round for agriculture.

### Broadening the Disciplines

Orden *et al.*, (2011) report several country studies on the impact of the agricultural support disciplines on domestic policy in each of the countries. Their broad conclusion is that the support disciplines in the WTO agreement were too porous to substantially reduce domestic support in the various countries.<sup>6</sup> The authors go on to show that the support disciplines contained in the draft modalities negotiated in 2008 in the Doha Round, while stronger, more complicated and more heterogeneous, are likely still too porous to induce sharp reductions in domestic support for agriculture. Essentially, they argue that countries have become very creative in designing domestic support programs that meet the criteria set out in the WTO agreement and are likely to be equally creative in policy design if the draft modalities of 2008 are confirmed in conclusion of the Doha Round. They suggest considerably greater transparency and timeliness in reporting existing and changed domestic policies so that all members have up-to-date information. Equally, countries have shown considerable variation on what is reported and how it is reported to the WTO.

One example is market price support. While the PSE method measures market price support for all production in the country, the Agreement on Agriculture allows the use of a smaller quantity, *viz.* the production eligible to receive the administered price. The WTO Appellate Body has ruled that this quantity can be less than total production if the government announces what the eligible quantity is. While countries are expected to measure such support in the same way as they did in the Uruguay Round, some countries have found ways to claim that they do not need to do so. The result is that some countries report only small levels of market price support, making it easy to stay below their WTO limits

even if the support activity impacts the national market as a whole.

Another example cited is that the US does not notify “irrigation subsidies related to maintenance and operating costs (which irrigators apparently pay), nor for the benefits of water charges to farmers that are below those for other users (which is a common practice)”<sup>7</sup>. The latter example above has a wider implication. If farmers are not paying for the natural resource (water) at reasonable market rates faced by other users in the economy, then a subsidy exists. Moreover, resources priced below rates that allow long term sustainability of the resource results in eroding the natural environmental capital in the US. Interestingly, the US used a similar argument against Canada to impose the softwood lumber tariff. The stumpage fees paid by timber companies harvesting on crown lands in Canada were administered prices, not established in an open marketplace as they were in the US. Such subsidies have the impact of lowering or suppressing world prices for commodities produced with the subsidies, thereby lowering the returns to other exporters around the world.

One of the underlying frustrations going forward is the range of issues that have emerged since 1995 under the WTO. Many of these issues have existed for years, long before the 1995 agreement, but were submerged beneath the tariffs, and domestic and export subsidies. As some of the tariffs and subsidies were reduced, these issues took on far greater importance and visibility. A few examples of these issues are sub-national support (tax breaks, green field plant subsidies provided by states, provinces, or municipalities), world price suppression from remaining direct and indirect subsidies, exclusion of various underpriced resources in agricultural production (e.g., water), as well as sustainable environmental services/impacts, from measurements and limitations on market distortions. There are issues in other pillars as well, such as national standards for environmental goods and associated product claims (and the problem of “greenwashing”), labour standards, and animal welfare. These have increasingly become market access issues, not contemplated under the existing pillars.

<sup>6</sup> The countries studied included European Union, United States, Japan, Norway, Brazil, China and Philippines.

<sup>7</sup> Orden *et al.*, 2011. Chapter 4, United States, pg. 127-128.

A second observation is that the framework and detailed outcome of the WTO agreement concerning support disciplines was largely written with the policies and programs of three countries in mind: USA, EU and Japan. A range of domestic and international measures were carefully designed to protect a number of politically sensitive issues within these countries. A good example is the blue box criteria developed in the Uruguay Round, which exempt certain payments that these countries could not come to agreement upon.

### Moving Forward

One could foresee two or more decades of trade litigation on a case by case basis to tackle these issues one-by-one within the WTO framework. The frustration will come from the way in which the WTO rules were designed to protect or minimize some of the issues; a case in point may well be the underpricing of water for agriculture in the USA, and not including such underpricing in the domestic (or export) subsidy levels. No nation has challenged the way the US has excluded this support to agriculture. Importers of US product enjoy the lower price and hence have no reason to challenge. Other exporters face the problem of the immense costs to raise a successful challenge.

During the Uruguay Round, after agreement on the structured approach for access, domestic and export support, it was recognized that the framework for the Uruguay Round negotiations in agriculture needed considerable work to deepen the knowledge base and measurement in order to have a transparent discussion of winners and losers, levels of distortion by type of subsidy, and trade regulatory systems such as sanitary and phytosanitary (SPS) to provide a comprehensive approach. The resulting assessments were balanced, nuanced, detailed and broadly accepted within the professional trade policy community involved and member countries.<sup>8</sup>

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<sup>8</sup> The International Agricultural Trade Research Consortium published a series of commissioned papers on major identified issues in agricultural trade policy over several years during the

What we do not have today is a comprehensive, detailed study of and proposals for the various issues noted above, building on what took place over 20 years ago. It is time to design a framework to deal with these issues on a multilateral basis, rather than the tackling the myriad of issues through trade litigation that Orden and others have identified. Such an approach would address many of the most politically toxic regional issues in several countries. Necessarily, this will be a long term endeavor, but hopefully less costly and more inclusive than setting precedents one-by-one through WTO litigation, not all of which would have successful outcomes across the range of issues.

### Conclusion

The design of the agri-food trade system, and the format within which we discuss and analyze it, is based on certain assumptions with respect to the nature of distortions from trade policy instruments, and limits placed on policy instruments upon which dialogue, disputes, and remediation can occur. As the world has evolved toward greater awareness of resource scarcity, increased demand for food, and greater influence of less developed and developing countries, many of these assumptions are less valid today. Moreover, it is clear that needed multilateral trade agreements are increasingly difficult to negotiate, in part because of the format of the pillars and the associated metrics and analysis.

Without exploration and refinement of trade disciplines, it will be increasingly difficult to address the trade skeptics and naysayers who argue that trade agreements on agriculture and food aren't fair because many of the real issues are left off the table. Canada needs to take this issue more seriously. Canadian agri-food was revolutionized by trade liberalization in the early 1990's, and this requires renewal. If aspects of proposed changes in supply management are challenged internationally, part of the defense of program changes and accommodation of supply-managed groups will need to be more effectively listening to their concerns about the

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Uruguay Round. Most can be found on ageconsearch. See: <http://ageconsearch.umn.edu/>

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structure of international trade disciplines and the actions of other countries under these disciplines. It will also be an element of legitimacy in public policy as domestic policy is restrained to pursue foreign markets, facing what appears to be increased agnosticism, if not outright opposition, to trade and trade agreements.

Finally, the immediate and mid-term outlook is for lower prices of many farm products, especially grains and oilseeds. Consistent with this, it can be anticipated that there will be increased claims under Canadian business risk management programming, and under farm subsidy programs employed in other countries. The bull market of 2007-13 took the emphasis off farm support programs as many were not in subsidy claim position due to high prices. It is an opportune time now to consider how countries are supporting agriculture and how this aligns with agreed upon commitments- both in strict magnitudes of support and in broader concept given the intent of the WTO agreement. This should lead to reconsideration and modernization of our framework for disciplines on agricultural support.

### References

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