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Staff Paper

Issues and Alternatives in the 1995 Farm Bill Debate: Implications of the Uruguay Round of GATT Negotiations

By

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Abstract

The recently completed round of negotiations under the General Agreement on Tariffs and Trade focused on domestic and international agricultural policies. If this agreement is approved by Congress, U.S. agricultural programs must comply with GATT provisions. The policy choices made during the 1995 farm bill debate about domestic programs, import policies, and export programs could all be affected by the approval of GATT.

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ISSUES AND ALTERNATIVES IN THE 1995 FARM BILL DEBATE: IMPLICATIONS OF THE URUGUAY ROUND OF GATT NEGOTIATIONS

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From the Series: Michigan Agriculture in a Global Economy

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The recently completed round of negotiations under the General Agreement on Tariffs and Trade focused on domestic and international agricultural policies. If this agreement is approved by Congress, U.S. agricultural programs must comply with GATT provisions. The policy choices made during the 1995 farm bill debate about domestic programs, import policies, and export programs could all be affected by the approval of GATT.

The Policy Framework Negotiated in the Uruguay Round

The Uruguay Round agreement requires the members of GATT to reduce expenditures on domestic agricultural programs and export subsidies. Members are also required to replace all import quotas with tariffs and reduce all existing and newly-created import tariffs. The basic framework of this agreement contains four elements:

- Domestic support programs for agriculture must be capped at their 1986-1988 level and reduced 20 percent by the year 2000.

- Export subsidy programs for agriculture must be capped at their 1986-1990 level and reduced. The volume of subsidized exports must be reduced 21 percent by the year 2000. The budgetary outlays for export subsidies must be reduced 36 percent by the year 2000.

- All existing import quotas must be converted into import tariffs. All existing and new tariffs must be reduced by an average of 36 percent, with a minimum tariff reduction of 15 percent for each product. Tariff reductions will be phased in by the year 2000.

- All countries must allow imports to have access to at least 3 percent of domestic consumption during the first year of the agreement, increasing to 5 percent of domestic consumption by the year 2000.

Implications for Domestic Agricultural Programs

Though the Uruguay Round agreement requires countries to reduce their domestic agricultural programs, the United States will not be required to alter the structure of its domestic programs or reduce existing levels of expenditures on domestic agricultural programs.

Existing U.S. target price and loan rate programs would continue if the Uruguay Round agreement is approved. The agreement requires that all domestic agricultural programs meet two criteria to satisfy the provisions of GATT.

First, the agreement requires that all domestic programs be "non-trade-distorting." To meet this requirement, programs must be based on fixed a volume of production (fixed areas and yields) and payments must be made on no more than 85 percent of production. Because U.S. program bases and yields are frozen and deficiency payments were limited to 85 percent of base acreage by the introduction of "flex acreage" in the 1990 farm bill, existing U.S. target price and loan rate programs would be permitted to continue if the Uruguay Round agreement is approved.

Second, the agreement requires all countries to cap their domestic agricultural programs at 1986-1988 levels and reduce expenditures on these programs by 20 percent by the year 2000. Countries that have reduced agricultural program expenditures since 1986 will receive credit for the reductions that have already been made. Because the United States has already reduced expenditures on commodity programs by more than the 20 percent minimum, the United States will not be required to make additional reductions in domestic commodity programs.

Several programs are classified as "non-distorting" by the Uruguay Round agreement and are not included in the program reductions required by the agreement. Research and extension programs, pest and disease control programs, inspection services, domestic nutrition program (the Food Stamp Program), crop insurance, disaster payments, environmental and conservation programs, "decoupled" direct payments, and income insurance programs are classified as non-distorting programs. The United States is not required to reduce expenditures on these programs.

These provisions would permit the United States to convert its commodity programs to either a "revenue assurance" program that provides payments to farmers if their revenue falls below a benchmark level or to a "green payments" program that provides payments tied to the use of specified production practices. Both of these programs have been proposed as alternatives to the existing U.S. commodity programs.

Implications for U.S. Export Policies

The Uruguay Round agreement would also require member countries to reduce their use of export subsidies. Each country would be required to reduce its volume of subsidized exports by 21 percent and its budget expenditures on export subsidies by 36 percent from the level that existed during the 1986-1990 period. These provisions apply to direct subsidies, disposal of government stocks below the market price, producer-financed export subsidies, marketing subsidies, and all transportation and freight subsidies.

These provisions of the Uruguay Round agreement will be applied to the U.S. Export Enhancement Program (EEP) and the Dairy Export Incentive Program (DEIP), with reductions in the maximum volume of subsidized exports and the maximum budget for export subsidies being established each year during the 6-year transition period (Table 1). Those products whose export subsidies increased after 1990 (dairy products and vegetable oils) must reduce their export subsidies by more than the required minimum (21 percent of volume and 36 percent of value) to comply with the Uruguay Round agreement. The United States would also be prohibited from using export subsidies on fruit products after 2000. No Export Enhancement Program subsidies were used on fruit in 1994 and none are expected in the near future.

The U.S. Market Promotion Program (MPP), which provides cost-sharing funds to firms and commodity organizations that implement foreign market development programs, and the P.L. 480 program, which provides food aid to developing countries, are not considered trade-distorting subsidies by the Uruguay Round agreement. The United States is not required to reduce these programs.

Implications for U.S Import Policies

The Uruguay Round agreement will also require all members of GATT to reduce their barriers on agricultural imports. All import quotas must be converted into tariffs, and all new and existing tariffs must be reduced by 36 percent by the year 2000. All products must have their tariffs reduced by at least 15 percent.

These provisions would be applied to the "Section 22" import quotas used by the United States if the Uruguay Round agreement is approved. These quotas were established under Section 22 of the Agricultural Adjustment Act of 1933, which permits the President to impose quotas if imports are found to interfere with U.S. price support programs.

Table 1. Maximum Level of Export Subsidies Permitted in 1995 and 2000 Under Provisions of the Uruguay Round Agreement.

	Maximum Volume of Subsidized Exports		Maximum Budget for Export Subsidies	
	1995	2000	1995	2000
	(Thousand Tons)		(Thousand Dollars)	
Wheat	22,309	16,008	765,499	363,815
Feed grains	2,101	1,721	67,735	46,118
Rice	300	43	15,706	2,369
Vegetable oil	647,650	155,755	52,960	14,083
Beef	24,543	19,389	28,889	22,822
Pork	551	435	629	497
Poultry	37,695	30,858	21,377	14,555
Cheese	4,221	3,340	5,340	3,636
Butter and oil	47,387	23,256	44,793	30,497
Nonfat dry milk	119,300	75,179	121,119	82,464
Other dairy products	13,730	38	14,374	21

The United States would be required to replace its import quotas on dairy products, sugar products, peanuts and cotton with tariff-rate quotas. Under a tariff-rate quota the importing country would permit a specified quantity of imports to enter duty-free (or, in the case of sugar, at a very low tariff). All additional imports would be assessed an over-quota tariff. The duty-free quota would increase and the over-quota tariff would be reduced (but not eliminated) during the transition period.

Dairy products: The United States would be required to provide duty-free access for 122,355 tons of imported cheese during 1995. All additional cheese imports would be subject to an over-quota tariff of 65.5 cents per pound. The duty-free volume would increase to 156,518 tons in 2000, and the over-quota tariff would be reduced to 55.7 cents per pound in 2000.

The United States would also be required to provide duty-free access for other dairy products equivalent to 15,102 tons of milk fat and 17,747 tons of nonfat solids in 1995. These quotas would increase to 25,116 tons of milk fat and 29,570 of milk solids in 2000. The over-quota tariffs on these products would also be reduced during the transition period. The over-quota tariff on nonfat dry milk would be reduced from 46.2 cents per pound in 1995 to 39.2 cents per pound in 2000. The over-quota tariff on butter would be reduced from 82.2 cents per pound in 1995 to 69.9 cents per pound in 2000.

Sugar: The United States has used a tariff-rate quota to limit sugar imports since 1990. All sugar entering the United States under the quota is assessed a tariff of 0.625 cents per pound. Additional imports are assessed an over-quota tariff of 17 cents per pound. The 1990 farm bill requires that imports be no less than 1.25 million tons annually.

Under the provisions of the Uruguay Round agreement, the United States must provide access for 1.23 million tons of raw sugar and 24,251 tons of refined sugar. The tariff on this in-quota sugar would remain at 0.625 cents per pound. The tariff on over-quota imports of raw sugar would be reduced from 16 cents per pound in 1995 to 14.45 cents per pound in 2000. Existing Section 22 quotas on sugar-containing products would also be replaced with tariff-rate quotas.

Other products: The Uruguay Round agreement would also require the United States to replace its Section 22 quotas on peanuts and cotton with tariff- rate quotas. The United States would provide duty-free access for 57,240 tons of cotton in 1995, with an over-quota tariff of 16.7 cents per pound applied to all additional imports. The duty-free quota would increase to 95,400 tons and the over-quota tariff would be reduced to 14.2 cents per pound in 2000.

The United States would also provide duty-free access for 37,225 tons of peanuts in 1995, with an over-quota tariff of 36.3 cents per pound for shelled peanuts and 23.9 for in-shell peanuts. The duty-free quota would increase to 62,041 tons in 2000. The over-quota tariffs would be reduced to 30.8 cents per pound for shelled peanuts and 20.4 cents per pound for in-shell peanuts in 2000.

Long Run Implications of the Uruguay Round: New Constraints on Agricultural Policy

The Uruguay Round agreement would impose some new constraints on U.S. agricultural policy. The United States would not be required to change its existing domestic commodity programs and would be permitted to adopt revenue assurance or green payment programs in the 1995 farm bill, but the provisions of the Uruguay Round would impose other constraints on the 1995 farm bill debate.

The United States would be required to reduce its use of export subsidies under the 1995 farm bill. The agreement would also prohibit the United States from using Section 22 import quotas to maintain domestic commodity programs. Given the existing level of imports and the structure of the tariff-rate quotas specified in the agreement, U.S. imports of sugar and cotton are not expected to change significantly if the agreement is approved by Congress. Consequently, domestic programs for these commodities are not likely to be affected by the approval of the Uruguay Round agreement. U.S. imports and exports of dairy products are expected to increase if the agreement approved and the use of U.S. dairy export subsidies would also be reduced significantly. Some studies suggest that the net effect of these changes could lead to an increase in government purchases of dairy products. The final impact of the agreement on the dairy industry will depend upon future decisions about the milk support price.

In the longer run, the approval of the Uruguay Round agreement will impose new constraints on agricultural policy decisions. First, the agreement's limits on the use of export subsidies imposes new constraints on the use of price support programs. Because governments will not be permitted to use export subsidies to dispose of government stocks accumulated under price support programs, policymakers will face tighter constraints that will limit their ability to establish price support levels above the market price.

Second, disposal of government stocks could become more reliant on food aid exports, which are usually more expensive than direct export subsidies. Again, policymakers' decisions about the use of domestic price supports will be constrained by their limited ability to dispose of excess stocks. Third, the opening of markets through the elimination of import quotas will also constrain the decisions of policymakers. Any decision to increase prices

through domestic price support or production control programs must consider the prospect that such a decision could result in increased imports or decreased exports, thereby resulting in a minimal impact on domestic price.

The Uruguay Round agreement probably provides an indication of the long run trend in agricultural trade policy. Future negotiations are likely to continue the reduction of export subsidies and import tariffs after the year 2000.