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Implications of the July 2004 WTO Framework Agreement for Canadian Agriculture

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1.0 Background

When the Uruguay Round of multilateral trade negotiations concluded in 1994, the World Trade Organization (WTO) Members mandated that new negotiations begin in 1999 for agriculture and services (WTO 1993). However, everyone knew that these sector specific negotiations would flounder unless they were part of a comprehensive trade round. As a result, the launch of a new round of WTO negotiations was expected during the Seattle Ministerial meetings in late 1999.

Despite the well publicized failure of the Seattle Ministerial technical discussions of issues surrounding the Agreement on Agriculture (AoA) began in March 2000 in Geneva. Finally, at the Doha Ministerial in November 2001 a new comprehensive round (the Doha Development Agenda (DDA)) of multilateral trade negotiations was launched. The Doha Ministerial Declaration set an ambitious target for the conclusion of the Round in 2005 (WTO 2001).

Unfortunately, there was insufficient political will to abide by the timetable set in Doha. The first major setback occurred in Cancun, in September 2003, when Minster's were unable to agree on the modalities (specific targets for commitments) for further negotiations. While the negotiations on agriculture were difficult most observers feel they were not the reason for the failure to reach a consensus. At the Cancun Ministerial the suggestion that the DDA should encompass government procurement, competition policy, investment and trade facilitation lead to a stalemate. Developing countries were adamant that these issues should not be on the table and the Cancun Ministerial was terminated with no agreement on the modalities.

It wasn't until July 2004 that a "framework agreement" for the agricultural negotiations was finally accepted as a guide for the future negotiations.[1] The July agreement provides guidelines for the negotiators in the areas of agriculture, non-agricultural market access, development, services and trade facilitation. The Framework Agreement also reflects the consensus of the General Council to continue the negotiations launched at Doha beyond the timeframe set out in the Doha Declaration. Currently, the negotiators are attempting to reach a consensus on a draft text for the modalities by the time of the Hong Kong Ministerial meeting scheduled for December 2005, with final approval expected sometime in 2006.[2]

The Framework Agreement for agriculture is the subject of this paper. It should be recognized that difficult negotiations lie ahead because the Framework Agreement does not set the depth of the cuts for tariffs or domestic support, or the specifics of other disciplines and the timing of the implementation.

In section 2 we discuss ten things that Canadians interested in the agricultural negotiations should know about the Framework Agreement, but first it is useful to review

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[1] The official WTO (2004a) document refers to the Framework Agreement as a "work programme" but we will use the more familiar term in this review.

[2] The requirement is to reach consensus in all areas of the negotiations, not just agriculture.

a few facts. One of the most important facts is that many of the problems that Canada faces in agrifood trade are not covered by the Agreement on Agriculture. Canadian exports of some agrifood products have been impeded through the use of contingency protection laws (countervailing duties and anti-dumping duties), especially by the United States. The negotiations on contingent protection laws are being conducted separately in the Negotiating Group on Rules and are governed by separate WTO agreements (Anti-Dumping Agreement and the Agreement on Subsidies and Countervailing Measures). Trade barriers associated with human, animal or plant health are covered by the Agreement on the Application of Sanitary and Phytosanitary Measures (SPS), whereas trade problems associated with packaging, labeling and technical regulations are covered by the Agreement on Technical Barriers to Trade (TBT) – neither of these agreements is being renegotiated during the Doha Development Round. The relevant WTO Agreements, relating to biotechnology, span the SPS, TBT and Trade-Related Aspects of Intellectual Property Rights Agreements. These important trade issues and WTO Agreements are reviewed by Gaisford and Kerr.

Before turning our attention to the Framework Agreement it is useful to review Canada's trade performance, its negotiating objectives and current levels of support and protection in the agrifood sector.

1.1 Trade Performance

Canada's trade performance is shown in table 1 from 1991 through 2003 (AAFC 2004b).[3] Between 1991 and 2002 Canada's total agrifood exports have more than doubled (133.3 percent) but most of that growth took place between 1991 and1996, with export sales only increasing by 28.9 percent between 1996 and 2002. However, these aggregate figures hide two extremely important trends in the data. First, almost all of the growth in agrifood exports was accounted for by sales to the United States where exports nearly tripled (286.6 percent) between 1991 and 2002. The growing importance of the United States market is illustrated by noting that the United States accounted for 40.5 percent of total agrifood exports in 1991 and this value reached 48.7 percent in 1996. By 2002, the United States accounted for 67.2 of Canada's total agrifood exports, and Mexico accounted for another 3.0 percent, rising from essentially nothing in 1991. Second, exports of bulk products that accounted for nearly 50 percent of Canada's exports in 1991 have fallen to 23.3 percent in 2002, having declined by \$2.1 billion between 1996 and 2003. Third, exports of consumer ready products have more than tripled since 1991 and the growth of exports outside the United States market has more than doubled, albeit from a small base. Canadians might still be "hewers of wood and drawers of water" but when it comes to agrifood exports they tend to be packaged, labeled and ready to be eaten by Americans. The positive side of this development is that much of the value added in food manufacturing is being captured in Canada, but it also means that the \$24.4 billion in agrifood exports has much less "farm" product in it than it did when most of the sales were of bulk commodities. In addition, Canada's prosperity is highly dependent on the United States market and the BSE crisis has

[3] In most of the comparisons we have chosen to use data for 2002 rather than 2003 because of the distortion caused by the BSE crisis.

taught us what can happen when the border closes to such an important trading partner (Caswell and Sparling).

Finally, it is not surprising that most of the growth in Canada's sales of products abroad has taken place in a market where we have tariff free and preferred access – namely the United States. Unfortunately, the tariff preferences which Canada has enjoyed in the United States market are being slowly eroded as the United States becomes more aggressive in seeking out bilateral trade agreements.

1.2 Support and Protection

The AoA imposed some constraints on support and protection in the agricultural sector but these disciplines are generally weak. In most developed countries the agricultural sector remains highly distorted regardless of the measure used.

The average bound tariff in agriculture is 62 percent compared to 3-4 percent in manufactured products (Figure 1) and average tariffs are high on nearly all products (Gibson, et. al.).[4] The highest average tariffs (over 80 percent) are on tobacco, dairy products and meat while even the "low" tariff products like nuts, fruits and horticultural products have tariffs exceeding 50 percent on average (Figure 2).

The OECD (2003) calculated that total support for its member countries equaled $240.8 billion in 1986-88 and even with more members it fell to $234.8 billion in 2002. Support, in dollar terms, is very high in the European Union ($100.5 billion), Japan ($43.9 billion), the United States ($39.6 billion) and Korea ($18.1 billion). For the OECD as a whole, support as a percentage of the value of production fell from 38 percent in 1986-88 to 31 percent in 2002. In percentage terms support remains very high in Norway (71 percent), Korea (66 percent), Japan (59 percent), and the European Union (36 percent). Overall support levels, in Canada (20 percent) and the United States (18 percent) have been similar for the past 20 years. However, these overall figures hide the fact that support in the United States is skewed very heavily towards rice (52 percent), sugar (55 percent) and milk (46 percent) and to a lesser extent wheat (30 percent), while Canadian support is skewed towards milk (55 percent) and eggs (28 percent) with most other Canadian commodities having support levels between 12 and 23 percent. The aggregate figures also hide the fact that the mix of policy instruments that countries use to support their agricultural sectors have also changed over the past 15 years. Market price supports[5] which in 1986-88 accounted for 61.6 percent of total support have dropped to 46.7 percent of total support in 2002. This is a positive development because consumers, especially low income consumers, bear less of the cost of protection.

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[4] The calculation of the average tariff is based on data from 129 WTO member countries (Gibson, et. al.).

[5] Market price support includes policies that maintain domestic prices for farm goods at levels higher than those at the country's border.

1.3 Canada's Role in the Doha Negotiations

Canada's official negotiating position was set out in August 1999 after extensive consultations with industry representatives and other levels of government.[6] Obviously, events have changed since this position was articulated but the basic objectives remain the same: elimination of export subsidies, maximum possible reductions in trade distorting domestic subsidies, and improvements in market access for Canada's exports of agri-food products. Canadian negotiators face a difficult balancing act between protecting Canada's import sensitive sectors and furthering the interests of its export sectors. In section 2 some of the possible trade-offs involved in the negotiations are examined. The core of the discussion is organized around the three pillars of the negotiations: export competition, domestic support, and market access. The trade-offs are addressed by highlighting ten important issues and asking what the implications are for Canada.

2.0 Will Export Subsidy Elimination Solve Canada's Problems in Agriculture?

An export subsidy is conditional upon the subsidized product being exported (Young, Abbott and Leetmaa). The WTO takes a broad view of the definition of an export subsidy; it includes direct payments, the granting of tax relief, the granting of low interest loans, disposal of government stocks at below-market prices, subsidies financed by producers or processors as a result of government actions, marketing subsidies, transportation and freight subsidies, and subsidies for commodities contingent on their incorporation in exported products (USDA 1993). Despite a long standing prohibition on subsidies for industrial products that are contingent on export performance (WTO 1994a, Article 3) these subsidies persist in markets for agricultural products. However, a major achievement of the UR is that it put limits on existing export subsidies and prohibited the use of new export subsidies. The Framework Agreement lays out a plan for the elimination of all forms of direct and indirect export subsidies in agriculture.[7] Subsidies subject to elimination include direct subsidies; government export credit arrangements with terms of more than 6 months[8]; government financing of exporting state trading enterprises (STEs) and underwriting the losses of these enterprises; and, food aid that is used as a means of surplus disposal or has the effect of displacing commercial sales (WTO 2004a). Also up for negotiation are the terms and conditions under which export monopolies can be used.

The experience since 1995 has been that Members have more than met their export subsidy commitments. Prior to the signing of the AoA most export subsidies

[6] Canada's official negotiating position can be found at http://www.agr.gc.ca/itpd-dpci/english/current/wto.htm

[7] Direct subsidies provide an explicit price subsidy to either the exporting or importing agent, lowering the price of the traded good. Indirect subsidies provide non-price benefits that ultimately lower the final cost to the importer.

[8] For loans under six months, additional disciplines will be negotiated with respect to minimum interest rates, insurance premium benchmarks and other loan conditions.

were used for grains. Subsequently, export subsidies for grains declined dramatically because the US stopped using the Export Enhancement Program and the European Union (EU) dramatically reduced its use of export restitutions. The EU was able to reduce their reliance on export subsidies because of domestic policy reforms that lowered internal support prices for grains.[9] Currently, despite its policy reforms, the EU is the only significant user of direct export subsidies and it now accounts for 91 percent of these subsidies (AAFC 2004a). Dairy products capture the largest share (34 percent) of total expenditures on export subsidies (WTO 2000a).

From a Canadian perspective does the elimination of direct export subsidies matter? Yes, there are two sectors that are directly affected by export subsidy elimination. First, although Canada is not a major player in international dairy markets, historically it has had to use export subsidies to export products that are surplus to its supply managed regime. Initially, surplus skim milk powder was sold internationally with subsidies financed by producer levies. Following the UR a new price discrimination system created a class of milk that was priced at international levels, and products made from this milk were exported. However, after a series of WTO dispute panels this regime was ruled an export subsidy. As Canada's export subsidies are eliminated, along with all other countries, exports of Canadian dairy products will be cut to virtually nothing with the exception of some high quality cheeses. The loss of the export market will put additional financial pressure on domestic milk producers and dairy processors. In the early 1990's Canada's milk and dairy product exports were valued around $150 million, they peaked in 2001 at $443 million on sales of 185 million metric tonnes, and then declined to $314.5 million in 2003 (174 million metric tonnes) as unit values dropped sharply. However, to put this in perspective, Canada's farm cash receipts from sales of milk and cream are about $4.5 billion.

Second, Canadian grain exports often have to compete against subsidized exports from the EU. The EU's recent use of export subsidies for grains has been sporadic but they may become more frequent given the recent strength of the euro. As recently as mid-February 2005 the EU employed a small restitution to make a wheat sale. Prior to this sale the EU had not used a wheat export subsidy since 2003. Despite reduced intervention prices, the increased value of the euro (relative to the US dollar) and increased transportation costs could create pressure for the EU to increase its use of export restitutions for grain. What is the probability that the EU will be forced to use export subsidies? A simplistic extrapolation of the potential use of EU export subsidies can be assessed by determining the probability that the EU intervention price for wheat will exceed the world price for a comparable grade of wheat. Our analysis suggests that the probability of the EU needing export subsidies is 15-30 percent depending on the exact assumptions used in the analysis.[10] So, from a practical standpoint there is value

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[9] Prior to 1992, the EU intervention price for wheat was 155 euro/mt and through a series of reforms it was reduced to 101 euro/mt in 2001.

[10] Distributions on the US Gulf price of soft red winter wheat and the euro/dollar exchange rate were obtained from weekly data for the period August 1, 1997 to February 4, 2005. Given these distributions, the probability of the intervention price exceeding the US Gulf price, adjusted for the euro/dollar exchange rate and transfer costs, can be determined.

in disciplining the EU in their use of export restitutions for wheat as well as to bring the rules for agriculture into conformity with the prohibition against export subsidies required in the rest of the WTO.

When will the elimination of direct export subsidies occur? This is one of the most important issues in these negotiations. The requirement for the parallel elimination of all forms of export subsidies, direct and indirect, is likely to prolong the process of eliminating export subsidies. However, a larger obstacle is the fact that the reform of the EU's agricultural policy will not be completed until 2013. There is a possibility that the negotiators may agree to a multiple track elimination schedule where export subsidies for some commodities (including grains) are eliminated relatively quickly (five years) and for other commodities, whose domestic prices are more out of line with international prices, export subsidies will be eliminated over a longer time period (10 years). Consequently, the most likely date for the complete elimination of export subsides is between 2015 and 2017, corresponding to about a ten year implementation period for the Doha Agreement.

Does the elimination of indirect export subsidies matter to Canadians? The OECD (2001) has estimated that the United States accounts for 46 percent of government sponsored credit programs and for 88 percent of the subsidy elements of these programs.[11] The same study showed that during 1995-98 Canada accounted 13 percent of the export credit programs used by OECD countries. Disciplines on subsidized credit will apply almost exclusively to programs for wheat exported by the Canadian Wheat Board (CWB) and this issue and the disciplines on financial assistance to the CWB are taken up in the next section.

The elimination of export subsidies, direct and indirect, will only have a small positive impact on world grain prices. The impact on international dairy prices is potentially much larger. However, the most fundamental benefit is that the reform will bring agriculture into conformity with the rules for industrial products and prevent any backsliding with respect to the use of export subsidies. The elimination of export subsidies will not solve Canada's problems in agriculture but it is a long overdue reform of international trading rules.

2.1 Will the Canadian Wheat Board be Eliminated?

The Canadian Wheat Board is western Canada's exclusive exporter of wheat and barley. As a government backed producer marketing board the CWB is classified as a state trading enterprise. STEs are permissible under the GATT (General Agreement on Tariffs and Trade) as long as they are in compliance with Article XVII that requires their practices to be consistent with non-discriminatory behavior and that their sales or purchases are made in accordance with commercial practices.

[11] The size of the subsidy element was considerably smaller than for direct export subsides and was approximately 6.6 percent of the export price.

The Framework Agreement only addresses exporting STEs and does not consider disciplines on importing STEs such as the Canadian Dairy Commission.[12] The proposed disciplines are to be applied under the export competition provisions of a revised Agreement on Agriculture. Article XVII is not being negotiated, so any new disciplines will apply only to agricultural STEs. The Framework Agreement calls for the end of "trade distorting practices with respect to exporting STEs including eliminating export subsidies provided to or by them, government financing, and the underwriting of losses". Disciplines on the length of term and other conditions for export credit sales provided through the CWB are also addressed in the Framework Agreement. Transparency provisions will be established that are consistent with commercial confidentiality considerations. Finally, the issue of whether state trading monopolies should be eliminated is under negotiation.

The operations of the CWB are based on three principles: single desk selling, price pooling and a government guarantee of the initial payment to producers. The Framework Agreement will result in the eventual elimination of the government guarantee for the CWB's borrowing and for the initial payment. Does the elimination of these guarantees affect the three core principles of the CWB?

The CWB borrows for a number of reasons: to finance its current operations, to finance its current credit sales, and to service old debt. In 2002/03 the CWB's net borrowing was $6.4 billion.[13] Borrowing to service old debt, associated with overdue and rescheduled debt from foreign customers was $5.87 billion. This old debt is associated with credit sales, under the Credit Grain Sales Program, which was guaranteed by the Government of Canada and the repayment terms were rescheduled through a forum known as the Paris Club. As such, this debt could be transferred to the books of the federal government and for all practical purposes the old debt is not relevant to the potential disciplines in the Framework Agreement.[14] The remaining borrowing of $558 million is associated with financing new credit sales and the operating expenses (inventory storage, inventory financing and grain movement) of the CWB.

The borrowing guarantee allows the CWB to obtain better financing than it could if it had to obtain funds commercially. The fact that the CWB owns only a few assets means that without the government guarantee its credit worthiness declines and its borrowing costs increase. The elimination of the federal government underwriting of losses affects the guarantee on initial payments. It is possible for the CWB to establish a contingency fund to backstop the initial payment. However, it will take time to build such a fund. Therefore, the CWB may seek a one time infusion of capital to help form a contingency fund and to help it reduce its borrowing costs. Although the CWB has generally been conservative in setting initial payments, without the government guarantee it will have to protect itself from sharp price declines after initial prices are

[12] The Canadian Dairy Commission has been granted the exclusive right to import butter; other dairy products are imported by the private trade under tariff-rate quota regimes.
[13] Goodloe reports that the gross borrowings of the CWB were $26.2 billion in 2002/03.
[14] The CWB benefits from the interest payments on this restructured debt. Goodloe claims that these interest earnings "more than covered the costs of running the CWB".

announced. Consequently, it will face additional costs associated with risk management. However, the tightening of the financial privileges that the CWB now receives is something that it can live with and price pooling and the provision of initial payments remain feasible.

The Framework Agreement calls for effective transparency provisions for export competition. The transparency provisions are to be consistent with commercial confidentiality. There are currently notification rules that require STEs to report on their activities every three years. The notifications involve a questionnaire concerning the products covered, the reason and purpose for the STE, a description of its functions and annual statistical information including product quantity and value, and trade flows. It is unclear what form new reporting requirements might take. The CWB is concerned about reporting information that may have commercial value to its competitors such as transaction specific prices. Typically, reporting requirements have involved yearly aggregations of data that the CWB already provides to producers.

The biggest issue with respect to the future of the CWB involves the negotiation of its continued monopoly status. The only WTO Member that is on record in for calling for an end of monopoly status for exporting STEs is the United States (USDA 2002). The EU is more interested in disciplines on STE behavior including cross subsidization, price pooling, and exporting at less than acquisition price (Abbott and Young 2004). Banning single desk exporting STEs would create an anomaly in WTO disciplines on STEs. First, paragraph 25 of the Framework Agreement would maintain monopoly status for developing country STEs that are used to preserve domestic price stability and to ensure food security. Second, STEs that export industrial products would not be subject to the same disciplines. Third, importing STEs (of industrial and agricultural products) would be allowed to continue their monopoly status. Effectively only Canada, Australia and New Zealand would be targeted by this discipline. This would move agricultural STEs, covered by the AoA, one step further from the GATT by creating an exemption to Article XVII. It is possible to consider arrangements where the private trade is given a role, but the STE continues to have exclusive control over most of the market. For example, ten percent of the export trade could be reserved for the private trade and the STE continues to have exclusive rights to the rest of the market. The issue of “monopoly elimination” may also be used as a negotiating chip to seek concessions elsewhere in the agricultural negotiations, so it is difficult at this point to speculate on the future of the CWB’s monopoly export status

The final issue that the CWB will face is increased disciplines on its use of export credits. The restriction of credit sales to a period of less than six months will not affect the CWB because virtually all of their sales are under this term limit.[15] Disciplines on credit sales under 6 months have not been specified, but probably will be similar to those contained in the Harbinson draft modalities (WTO 2003). The requirement that interest rates on credit sales be based on market interest rates should not pose a problem for the CWB. However, of the two credit programs used by the CWB for its credit sales (the Agriculture Credit Facility and the Credit Grains Sales Program) neither

[15] This information was obtained from personal communication with Kurt Denisuik of the CWB.

assesses an insurance premium for guaranteeing the credit transaction. A minimum insurance premium is one of the disciplines on credit programs that were contained in the ill fated Harbinson draft modalities (WTO 2003).

2.2 Can Market Access be Liberalized While Sensitive and Special Products are Given Special Treatment?

Market access issues have been at the center of eight previous Rounds of GATT negotiations. It was not until the eighth Round that the liberalization of border measures for agricultural products was seriously considered. Prior to the Uruguay Round, import quotas, variable import levies, voluntary export restraints, and other non-tariff barriers proliferated in agriculture. The accomplishments of the AoA include the conversion of non-tariff barriers into tariffs (tarifficiation); the binding of all agricultural tariffs where before many tariffs could be freely increased; the reduction of bound tariffs by an average rate of 36 percent (24 percent for developing countries); the creation of minimum access commitments through a system of tariff rate quotas[16], and the establishment of a special agricultural safeguard.[17]

While the AoA put into place a framework to begin market access liberalization and limited the types of border protection that could be used, not much liberalization took place and many technicalities allowed Members to get around the spirit of the AoA disciplines. Following the Uruguay Round Gibson, et al. found that the global average agriculture tariff equaled 62 percent. The tarifficiation process gave Members considerable discretion in converting quantitative border measures into tariff equivalents and minimum access was, in many cases, established at less than five percent of base period domestic consumption (Canadian Broiler Hatching Egg Marketing Agency, et al.). Many Members chose to bind the tariffs of their most import sensitive goods at extremely high levels and to reduce these tariffs by the minimum allowed reduction (15 percent). The introduction of new and inflated tariffs led to increased disparities in the level of protection between countries and across commodities.[18] Tariffs distort resource allocation and lead to overall welfare losses. These distortions are a function not just of average tariff levels but also of the differences among these tariffs across products. Tariff escalation, or charging higher duties for more highly processed products, is not just a problem for developing economies that are attempting to increase their value-added but it is also a problem for developed countries such as Canada that are increasingly exporting consumer ready products. The problem of tariff dispersion has led to calls for the harmonization of tariff structures where commodities or countries with higher levels of protection will have to make larger tariff cuts.

[16] A tariff quota is a two-tier tariff where one part has a low preferential tariff and the other part has a significantly higher (often prohibitive) tariff (Moschini). The quota limits the low tariff access.
[17] The special agricultural safeguard is discussed in section 2.5. It was designed to counter import surges and dramatic price declines by triggering increased tariffs under specified conditions. The special agricultural safeguard can only be applied to those commodities where a tariff equivalent was created from a quantitative measure.
[18] It might be argued if the disparity in protection levels went up following tariffication, but there is no argument that the transparency of differences in protection levels was greatly improved.

The Framework Agreement calls for substantial improvements in market access for all products.[19] The Framework does not define what "substantial" is, but it commits negotiators to reducing bound rates using a tiered formula that would make deeper cuts to higher tariffs. The degree of harmonization and the depth of the tariff cut will depend on whether a product is classified as a non-exempt, a "sensitive", or a "special" product.

Most agriculture products will not be subject to any special exemption. Market access liberalization for these products will involve a progressive system of tariff reduction, with deeper cuts for higher tariffs. The exact size of the tariff cut will be determined by the level of the current bound tariff and the development status of the country. However, the parameters for tariff reduction have yet to be negotiated and, although it is mentioned in the Framework Agreement, no decision has been made as to whether there will be a maximum allowed tariff. The Framework Agreement does not discuss expanding tariff rate quotas for any "tariffied" commodity that may be included in the non-exempt category.

Members can self select an *appropriate number* of sensitive products that will be given special consideration in the application of the tariff harmonization formula. The only selection criterion appears to be to take "account of existing commitments for these products" (WTO 2004a). Presumably the list of "sensitive" products will include, at most, those products already protected by tariff rate quotas. However, only 50 percent of the TRQs notified to the WTO actually utilized the quota restriction and remaining cases are administered as simple tariffs and some of these products may not be notified as "sensitive".

The Framework Agreement stipulates that "substantial improvement" in market access will apply for these sensitive products, but it does not explain how this improvement will be less substantial than for non-exempt products. The improvement is to be accomplished by a combination of tariff cuts and expansion of tariff rate quotas. This suggests that the smaller the tariff cut the bigger the expansion of the tariff quota. Although TRQs cover only six percent of the tariff lines they are prevalent in the sensitive sectors of dairy, sugar, meats and cereals (Meilke, et. al. 2001). The average over-quota duty, for all Members notifying TRQs, is 128 percent (Gibson et al.).[20] Given the very high over-quota rates it is likely that, at best, tariff liberalization will only take the "water" (or redundant protection) out of the tariffs and effective liberalization will depend on quota expansion.[21]

In the Uruguay Round Members were given a great deal of latitude in setting their minimum access commitments and as a result the actual preferential access

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[19] Least developed countries are exempt from making any reductions in their tariffs.

[20] The effective level of protection is much higher considering that roughly one-half of the TRQs are administered as simple tariffs.

[21] Currently, most over-quota tariffs are so high they can be lowered substantially without lowering domestic prices, the difference between the border price adjusted by the over-quota tariff and the domestic price is the "water" in the tariff.

created was much less than envisioned.[22] The effectiveness of liberalizing TRQs depends on which of its three instruments (in-quota tariffs, over-quota tariffs, or quotas) is the binding constraint. Skully argues that for the 25 percent of TRQs with low fill rates, the in-quota tariff is the binding constraint and it should be lowered in order to increase access. Fifty percent of the TRQs have fill rates over 80 percent, in these cases the quota can be considered the binding constraint and it is the instrument that should be liberalized. In this case reducing in-quota tariffs does not improve access but it does increase the profits of agents with the right to import.

Special and differential treatment will be available to developing countries in terms of smaller tariff reductions and quota expansions; access to a yet to be defined Special Safeguard Mechanism (section 2.5) and in their capacity to select an appropriate number of “special products”. These “special products” will enjoy still greater flexibility. Unlike “sensitive products” there are criteria for selecting “special products” and these criteria include food security, livelihood security and rural development needs. The Framework Agreement does not provide any definition of what livelihood security is, but the term definitely has protectionist connotations. The treatment of these “special products” will be defined in the next stage of the negotiations.

A trade round will ultimately be judged on the basis of improvements in market access. As a major agrifood exporter Canada has a huge stake in pushing for improved market access especially for consumer ready products. This means Canada should be a strong proponent for using a harmonization formula for tariff reductions and for rules to reduce tariff escalation. It should not be forgotten that Canadian consumers will benefit as Canada’s tariffs come down and a greater variety of lower cost imports are made available. From this perspective the creation of a new class of “special” and “sensitive” products is troubling. While Canada’s producers of supply managed commodities have a vested interest in maintaining protection for their commodities, the creation of a set of “special” products risks creating a permanent set of commodities where serious trade liberalization will be delayed for decades. Since sugar and rice will be prominent among the list of special products in developed countries it sends the wrong signal to developing countries that have a comparative advantage in producing these crops. At the very least, the number of tariff lines given special treatment must be very limited, in-quota tariffs for these commodities reduced to zero and meaningful minimum access commitments created.

Much of what is said above also applies to the sensitive commodity category available only to developing countries. However, in some cases developing countries are highly dependent on the production and/or consumption of one or a few commodities. Lower reduction commitments for these commodities might be justified, but again the number of tariff lines covered should be minimized.

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[22] Boughner, de Gorter and Sheldon provide reasons why minimum access opportunities are effectively not equal to five percent of base period consumption.

The market access portion of the Framework Agreement is its least precise element and the negotiations might run aground when the negotiators attempt to agree on the depth of tariff cuts and the number of special and sensitive products. Sensitive products are a category that was not envisaged in the Doha mandate; it extends special and differential treatment to developed countries resulting in pressures for maintaining protectionist measures everywhere.

2.3 What are the Expected Impacts on Supply Management?

The impact of the Framework Agreement on Canada's dairy and poultry sectors will be different so each sector is considered in turn below.

Mitchell argues that international dairy markets consist of two broad types: "controlled access markets" (North America, Europe and Japan) and "competitive supply markets" (New Zealand, Australia, Latin America, Russia and former Soviet Union Republics, North Africa, Middle East and Asia). International dairy markets are very thin with about five percent of world dairy production traded. For "controlled access markets" most dairy products will likely be designated as sensitive products. Table 1 shows that for these "controlled access" markets, not all dairy products have minimum access commitments equal to five percent of consumption.[23]

Table 1: Import Share of Domestic Consumption[24] – 1999.

	SMP	Butter	Cheese
Canada	0%	4%	7%
EU	8%	6%	2%
Japan	21%	34%	83%
US	1%	3%	5%

Source: Shaw and Love

The most likely outcome of the market access negotiations for "sensitive" products is some increase in minimum access commitments (for instance between 7 to 10 percent of an updated base level of consumption). The reduction in over-quota tariffs is unlikely to result in much improvement in access. Since fill rates are approximately 100 percent for dairy products, any reduction of in-quota tariffs will not affect trade flows but will increase the profitability (import quota rents) of those licensed to import the product. Incremental increases in minimum access combined with export subsidy elimination can nonetheless have a significant impact on world dairy prices given how little is traded.

[23] On a milk equivalent basis the share of market access relative to 2000 domestic consumption is four percent in Canada, 2.75 percent in the US and three percent in the EU (Canadian Broiler Hatching Egg Marketing Agency, et. al.).
[24] TRQ fill rates for all these products are effectively 100 percent so these percentages represent the maximum access at preferential in-quota duties.

The Canadian dairy sector will have to adjust to the elimination of export subsides, modest expansion of tariff quota volumes and a ceiling on product specific domestic support that will limit increases in support prices for the dairy sector. Since the WTO panel ruling on Canadian dairy export practices, it is nearly impossible for Canada to export dairy products. Canada's export subsidy commitments currently limit subsidized export volumes to 44.9 thousand tonnes of skim milk powder, 3.5 thousand tonnes of butter, 9.1 thousand tonnes of cheese and 30.2 thousand tones of other dairy products. Canada has not notified export subsidies since 1999 and consequently it is difficult to determine the exact quantities of subsidized dairy products. Nonetheless, total exports of skim milk powder have seldom exceeded the volume commitment and this is not a significant amount of skim milk powder to absorb into the domestic market. Exports of butter in recent years have been tiny, and although cheese and other dairy products are exported in higher volumes some of this product is sufficiently unique not to require subsidization. An increase in market access commitments will create some additional pressure for adjustments in the domestic dairy market either through a corresponding reduction in domestic production or a decline in domestic prices. Lariviere and Meilke, using 1995 data, suggest that requiring a minimum access commitment of seven percent of domestic consumption under dairy product TRQs could lower Canada's butter and cheese prices by 11 and one percent respectively and increase skim milk powder prices by two percent. Finally, the product specific ceilings on domestic support may not affect current dairy pricing policies, but the ceilings could constrain future increases in dairy support prices (section 2.4).

The situation facing the poultry sector is somewhat different. This sector will not face pressures from a cap on product specific AMS support as there is no notified market price support for these commodities.[25] Likewise, this sector will not face disciplines on export subsidies.[26] Market access as a percentage of domestic consumption is also higher for poultry than for dairy. In 2000, imports as a percentage of domestic consumption were 7.5 percent for broilers, 21 percent for hatching eggs, and five percent for turkeys and for eggs (Canadian Broiler Hatching Egg Marketing Agency, et al.). As a consequence these sectors should face less pressure from liberalized market access. During the early 2000's Canada's chicken prices were 15-20 percent above those in the United States; however with the recent strength of the Canadian dollar the price gap has increased to around 30 percent (Huff, Meilke and Amedei). Canadian milk prices, at the producer level, are about 40 percent higher than in the United States which is also a highly protected dairy market (Meilke, Sarker and Le Roy).

2.4 Does Domestic Support Really Matter?

Traditionally the WTO is concerned with trade policies and has not been very involved with domestic production policies except when they had a trade impact. The AoA however, disciplined domestic support measures that favour agricultural producers.

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[25] There is no administered price for any poultry product and consequently no AMS is calculated.

[26] Since domestic prices are higher than international prices there is some potential for a WTO panel ruling similar to that faced by the dairy sector.

In this respect, it is unique in that it contains explicit disciplines and reduction commitments on domestic support while industrial subsidies are constrained only by the provisions of the Agreement on Subsidies and Countervailing Measures. All domestic agricultural support is categorized as either subject to reduction commitments or not subject to reduction. Exempt programs include expenditures that are consistent with Annex 2 of the AoA (green box programs) or direct payments that are related to production limiting programs (blue box programs).[27] For non-exempt programs a quantitative measure of the level of support is calculated using an aggregate measurement of support (AMS). For developed countries product specific AMS that is less than five percent of the value production for the specific commodity is excluded from this calculation and therefore exempt from reduction. Furthermore, non-product specific AMS that is less than five percent of the overall value of agriculture production is eliminated from the calculation and also exempt from reduction commitments. All AMS that is less than the five percent threshold is *de minimis*.[28] The reduction commitment in the AoA, for developed countries, was a 20 percent reduction from 1986-88 AMS levels.

Given these disciplines is it necessary to seek further reform of domestic support? Empirical studies have shown that liberalizing tariffs generates significantly larger welfare gains than reductions in support policies (Hoekman, Ng and Olarreaga). The pre-AoA situation was that developed countries used very high levels of domestic agricultural subsidies. For the US and the EU this support involved intervention purchases that, in turn, required border protection to prevent erosion of support prices as a result of imports. Surplus stocks were sold on world markets through the use of export subsidies or given away as food aid. The domestic support disciplines were designed to reduce these types of distortions and to encourage reform away from the most trade distorting types of support to more neutral measures. The post-1995 experience is that both the EU and US have reformed their domestic agricultural policies towards less trade distorting measures. If all border measures and export subsidies were eliminated, then the potential for domestic measures to distort trade is greatly limited. However, comprehensive liberalization of all border measures will not happen during this Round and the success of a balanced agreement will entail greater disciplines on the provision of trade distorting domestic support.

The Framework Agreement preserves the fundamentals of the AoA disciplines on domestic support but adds several new requirements. First, there is to be a reduction in total support (that is the sum of final bound total AMS plus both *de minimis* exemptions and blue box support). This reduction comes in parts. In the first year of the implementation period Members must reduce total support by 20 percent. Additional reductions in total support are based on a tiered formula that encompasses the principle

[27] Green box programs or minimally trade distorting programs must be government financed and cannot involve price support. These programs include public goods (research, extension, inspection etc.) and direct payments to producers where the amounts are tied to fixed criteria and producers can not change their actions to alter their payments.
[28] *De minimis* provisions for developing countries are more generous with the threshold of ten percent for non-product specific and product specific support.

of harmonization where Members with higher levels of support face larger reduction commitments. Second, the final bound AMS and permitted *de minimis* levels will also be reduced over the implementation period. Tiered harmonization reductions would also apply to the total AMS (but not necessarily the same formula as for total support). Caps on support levels for specific commodities are to be negotiated to prevent shifts of support between commodities. Reductions in *de minimis* support will also be negotiated. Third, blue box support will be capped at five percent of a Member's average historic total value of production.[29] The blue box criteria are also being renegotiated. The Framework Agreement describes two types of blue box programs, direct payments that are either associated with production limiting programs (requires production) or payments that do not require production at all. Fourth, green box criteria will be reviewed and clarified to further remove its trade distorting elements but at the same time taking into account non-trade concerns (section 2.6)

Only 24 percent of the WTO membership currently has explicit domestic support commitments. From the perspective of many Members, especially developing countries, a successful Round will depend on how much additional discipline is applied to the domestic programs in the EU and the US. The major development in the Framework Agreement is the commitment to reduce total non-green support. In a sense, this overall limit is the price that the EU and US have to pay in order to not face reductions in green box support. If the overall commitment is the binding constraint then other Members may view the DDA as a success if the overall limit imposes indirect disciplines for spending on the individual domestic support components. For instance, a sufficiently aggressive reduction in overall support will create an effective limit on blue box support well below the 5 percent cap.

However, unilateral policy reform by the EU and US may mean that any new domestic support disciplines will not have much bite. For instance, while the EU-15's five percent cap on blue box payments is less than the 8 percent of its value of agricultural production that was notified in 2001 as blue box support (23.7 billion euros), recent reform of the EU's agriculture policy transfers most of these payments to the green box.[30] Furthermore, the initial down payment of a 20 percent reduction in total support will also not be binding for the EU because of agricultural policy reform. While it is likely that the EU will be included in the tier with largest reduction commitments for the AMS and total overall support, the reductions will have to be very aggressive or the EU will be left with significant breathing room.

The EU-15's existing bound commitment for total AMS support is 67.2 billion euro. In its 2001 notification the EU reported 39 billion euro in total AMS spending

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[29] The historic period is not specified and Members are allowed the greater of five percent of their average historic value of production or their existing blue box payments in establishing the base for overall reduction.

[30] In 2003-04 the EU introduced direct payments that are based solely on the fixed criteria of historic payments. The single farm payment should allow the EU to transfer most of the former system of compensatory payments into a fixed payment that the EU should be able to notify as consistent with Annex 2 of the AoA. Member States of the EU are allowed to keep up to 25 percent of existing crop specific compensatory payments (Kelch and Normile).

(WTO 2004b). However, by the time that a new trade agreement is implemented total AMS spending will be significantly reduced because of reforms in intervention prices for a number of major commodities.[31] Therefore, the reduction required in the maximum allowed AMS spending will have to be dramatic in order to impose effective disciplines on EU spending. Furthermore, the required reduction commitments for overall EU support will have to be even more ambitious to have any impact. Overall support includes blue box, AMS and *de minimis* support. Since the EU will reclassify most of its blue box support as measures claimed as green and since the EU has historically notified less than 800 million euro of *de minimis* spending[32], it would appear that the EU will have even more flexibility with respect to overall support than it would appear to have for any AMS commitment.

The Framework Agreement also gives the US a great deal of flexibility in meeting any future domestic support commitments. The redefinition of the blue box will allow the US to include its countercyclical payments in a category of support that is not subject to reduction commitments. In fiscal year 2005 countercyclical payments are projected to be US$3.9 billion (USDA 2005). These payments can vary over time depending on market prices, but the range in which the crop specific payment rate can vary is relatively narrow, areas and yields are fixed, so total expenditures will vary in a rather narrow range. If all the commodity prices are at or below loan rates the maximum countercyclical payment is roughly US$ 7.5 billion.[33] With five percent of the value of production as a cap on blue box payments the upper limit will be in excess of $10 billion. So the US will have ample blue box room.

The initial down payment of a 20 percent reduction in total support will not be binding on the US farm budget. Starting from a US$48.2 billion base the cap on US farm spending would be US$38.5 billion while current spending is roughly one half of this amount.[34] The US is likely to face a less aggressive reduction commitment for its AMS and its total overall support, than the EU, because of its historic spending level. The AoA final bound rate for the US total AMS is US$19.1 billion. In 2001, the Unites States notified AMS level was US$14.6 billion (WTO 2004c). Forty percent of this support is market price support for dairy and sugar which should remain relatively constant. Fifty-six percent of this support is made up of loan deficiency payments. The size of the loan deficiency payments depends on the level of international commodity prices and how much these prices fall below the loan rates after the DDA agreement is implemented. With modest reductions in the allowed AMS and relatively strong commodity prices the US should have ample breathing room. Even if the AMS commitment is binding and the loan rates have to be reduced, the countercyclical payments will increase. With blue box payments caped at five percent of domestic production there will be ample room for the increased countercyclical payments.

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[31] Relative to 2001 the following reductions in intervention prices will have been made (Kelch and Normile): rice (50%) sugar (33%); skim milk powder (15%); butter (40%) and beef (48%).
[32] This is less than ten percent of what they could be using for *de minimis* support.
[33] Personal correspondence with Paul Westcott, Economic Research Service, USDA.
[34] The overall spending of $48.2 billion is equal to $19.1 plus $21.9 as a maximum allowance for blue box and product specific and non-product specific *de minimis* support.

The impact of potential new WTO disciplines on Canada's domestic support expenditures is more difficult to assess (table 2). Canada has not notified domestic support since 2000. At that time domestic amber box spending was 21 percent of the AoA bound AMS limit. Since then government expenditures have increased as a result of BSE related expenditures and the introduction of the Canadian Agricultural Income Stabilization (CAIS) program. At this time it is not clear how Canada will notify its CAIS payments. Annex 2 of the AoA requires that payments be determined by income losses that exceed 30 percent of average gross income. However, the CAIS program begins to pay once the production margin falls below a reference margin based on an average of past margins.[35] Canada his historically notified most of its safety net spending as non-product specific *de minimis* expenditures, but potential reductions in *de minimis* support may offer less opportunity to use this reporting option. Another important issue for domestic support reform facing Canada is the constraints on product specific support which may put pressure on market price support for dairy and certain product specific provincial programs.

Table 2: Domestic Support Provisions of the Uruguay Round Agreement on Agriculture and the Doha Framework Agreement

	Uruguay Round	**Doha Framework Agreement**
A	Product specific support of five percent is exempt from reduction commitment.	Reduced over implementation period.
B	Non-product specific support of five percent is exempt from reduction commitment.	Reduced over implementation period.
C	Green box programs are exempt from reduction commitments.	Green box criteria to be reviewed and clarified to remove trade distorting elements and also to take into account non-trade concerns.
D	Blue box programs are exempt from reduction commitments.	Blue box support caped at five percent of historic average value of production or current spending levels. Blue box criteria are to be renegotiated.
E	Aggregate Measure of Support is cut by 20 percent.	AMS reduced over the implementation period.
F	No product specific AMS cap.	Product specific AMS ceiling to be negotiated.
G	No constraint on the total level of support provided through programs (A+B+D+E).	Support provided through programs (A+B+D+E) reduced by 20 percent in first year of implementation and subject to tiered cuts thereafter.

[35] A production margin is equal to allowable commodity sales less allowable expenses plus an accrual adjustment.

The Framework Agreement has added more structure to the existing domestic support disciplines with disciplines on overall trade distorting support and limits on blue box expenditures (table 2). However, how effective the disciplines will be in limiting trade distorting support is yet to be determined and it will depend on how aggressive the tiered formula reductions are for overall and total AMS support. One thing is fairly clear – the domestic support disciplines will not sharply limit spending on the agricultural sector by developed countries willing to shift support into the blue and green boxes. As a result, subsidy envy by producers in some developed countries and most developing countries will continue unabated. The fact that many of these subsidies are minimally trade distorting and quickly capitalized into land and other asset values, and hence cost structures will be ignored. The existence of large government expenditures in a few countries will result in lobbying for subsidies, of a corresponding size, by producers in other countries who see themselves as disadvantaged.

2.5 Developing Countries: Free Riders or Contributors?

Developing countries established at the Ministerial meetings in Seattle and Cancun that there will be no new trade agreement unless it offers them benefits that they perceive were not forthcoming from the Uruguay Round Agreement. However, the developing countries are not a homogeneous group and they do not speak with one negotiating voice. The Cairns Group has a number of developing country members who favor deep cuts in agricultural subsidies, while the G-10 has a few developing country members who argue against tariff caps, favor minimal market access improvements for special products and want non-trade concerns to be reflected in every aspect of the negotiations.[36] The G-20 consists entirely of developing countries, including India and China. The G-20 argued in Cancun for substantial cuts in agricultural support programs (WTO 2003).[37]

It is only a small exaggeration to say that many developing countries would favor an agreement that forces major market reforms in developed countries but exempts developing countries from making any significant contribution. This negotiating stance fails to recognize that bound tariffs in developing countries are very high, and there is much to be gained from increased South-South trade. For example the World Bank shows that 56 percent of the growth in agricultural exports, by developing countries, is to other developing countries. Many of the problems developing countries face in trading with the developed world are lessened when they trade with a neighbor, if they have reasonable access to the neighbors market.

A successful DDA depends on the good will and the actions of both developed and developing countries. The WTO and its rich Members have an obligation to further integrate the developing world into the world trading system but the developing country

[36] The G-10 includes Bulgaria, Iceland, Israel, Japan, Korea, Liechtenstein, Mauritius, Norway, Switzerland and Chinese Taipei.
[37] The G-20 includes Argentina, Bolivia, Brazil, Chile, China, Colombia, Costa Rica, Cuba, Ecuador, El Salvador, Guatemala, India, Mexico, Pakistan, Paraguay, Peru, Philippines, South Africa, Thailand and Venezuela.

Members have an obligation to contribute to the opening of markets (McCalla). The Framework Agreement does pay heed to the concerns of developing countries. The provisions of the Framework Agreement with respect to special and differential treatment includes the following considerations:

- The least developed countries will have full access to all special and differential treatment provisions and are not required to undertake reduction commitments with respect to market access or other forms of support. Developed countries and developing country Members in a position to do so, should provide tariff free and quota free market access for products originating in least developed countries.

- There will be a special sectoral initiative on cotton to address the problems in this commodity sector that are of vital importance for developing countries.

- Developing countries will be granted longer implementation periods and lower reduction commitments for all forms of trade distorting domestic support, export subsidy and tariff reductions.

- Developing countries will be exempt from reductions in *de minimis* levels of domestic support if most of the support is allocated to subsistence and resource-poor farmers.

- State trading enterprises in developing countries will be given special consideration for maintaining their monopoly status.

- Developing country Members can designate a number of products as special products that will receive more “flexible” treatment in the market access negotiations.

- Trade in tropical agricultural products will be addressed with the aim of achieving the fullest liberalization possible.

The above list is a long, but not exhaustive outline of negotiating issues where developing and least developed countries receive special and differential treatment in the Framework Agreement. The developing countries rightfully want an open, rules-based, transparent trading system where they obtain some of the gains from freer trade. They want protection from export embargo’s and export taxes and they want to be able to export to developed countries without undue worry about sanitary and phytosanitary rules, and technical barriers unjustly inhibiting their exports. The poorest developing countries will require assistance to develop their infrastructure to better reach far away markets. Finally, developing countries need assurance that environmental and labor standards will not be used to blunt their comparative advantage, nor will contingency protection laws be used arbitrarily to stifle their exports. Canada should endorse this trade friendly agenda because it is consistent with an export oriented economy.

Canada will also reap benefits as developing countries become richer. Developing countries are likely to be our future growth markets, especially for bulk products. However, in return for improved market integration it is reasonable for Canada, and other developed country Members, to ask that developing countries contribute to the successful conclusion of the DDA. They can make a major contribution in the following ways.

First, the structure of the commitments for developing countries should be the same as for developed countries (International Food and Trade Policy Council). While the commitment levels will be lower and the implementation period longer the structure of the commitments should be the same. Developing countries should agree to a ceiling on bound tariffs, especially given the huge gap between bound and applied tariffs in many low income countries. The creation of a class of "special" products is not a good idea because it locks-in permanent high cost production and taxes low income consumers (section 2.2). Unfortunately, it will difficult for many developed countries, including Canada, to speak against special products when they want to create a class of sensitive products to protect their own high cost producers. At the very least the number of special and sensitive products should be kept to an absolute minimum and it should be agreed that this is a temporary dispensation from normal WTO disciplines.

Second, there should be no blanket exemptions from WTO commitments. It would seem reasonable to make even least developed countries make a modest commitment.

Third, the issue of non-trade concerns (section 2.6) must be handled very carefully or it will open a huge loop hole in the Agreement. In general, non-trade concerns are best addressed using domestic support rather than border measures and some flexibility in this direction for developing countries would not be worrisome (Paarlberg, Bredahl and Lee). However, creating a class of border measures that are allowed for non-trade reasons is again likely to create a class of goods with very high protection levels largely impervious to change.

Finally, developing countries are being offered one additional instrument to protect their economies from a sharp increase in imports or a sharp decline in import prices. This instrument is called a Special Safeguard Mechanism (SSM). The SSM is pattered after the Special Agricultural Safeguard (SSG) introduced in the AoA and it is worthy of attention because the SSM's short-run impact will be to reduce imports by developing countries. This raises the question of whether Canada should support its introduction. The special agricultural safeguard introduced in the AoA differs from the other WTO safeguard mechanisms in that exact conditions are specified, with respect to the degree of import surge or import price decline required, to "trigger" the safeguard. Once triggered, the country has the right to raise tariffs on the effected commodity by the amount specified in the AoA. The application of the SSG is voluntary (i.e., a country does not have to charge the additional duty when triggered), and the country does not have to prove injury or compensate exporters. As a result, the SSG provides quick, relatively transparent protection against import surges and import price declines. Of the

148 current members of the WTO only 39 countries reserved the right to use the SSG, of which 29 are developing countries. However, from 1995-2000, the use of the SSG was dominated by three developed countries (WTO 2000b).[38]

The continued use of the SSG is under discussion in the DDA but developing countries have asked for a Special Safeguard Mechanism (SSM) that they could use. The Framework Agreement indicates acceptance of this idea "A special safeguard mechanism will be established for use by developing country members (WTO 2004a)" but no details are provided.

A SSM is a temporary duty and it has exactly the same effects as an increase in a tariff. It raises prices in the importing country, restricts imports and thereby reduces exports and world market prices. As a major exporter of agricultural products should Canada support the establishment of an SSM for use by developing countries? On the face of it the answer is no – why should Canada support measures that harm our exporters? However, there may be a trade-off worth making. If the establishment of an SSM allows developing country exporters to reduce tariffs more than they otherwise would, then Canada might come out ahead. In a study looking at the world wheat market Grant and Meilke conclude that the costs of an SSM are a small price to pay for aggressive tariff cuts in this sector. The benefits are less obvious if the tariff cuts are modest. Of course, the devil is often in the details. The negotiators must make sure that the price and quantity triggers for the SSM are reasonable and that the increases in duties allowed under the SSM are in fact temporary.

2.6 Green Boxes, Non-Trade Concerns and WTO Panels

The current green box criteria can be categorized into roughly two components: a number of general services with public good aspects (research, inspection, extension and training) and direct payments to producers (decoupled payments, structural adjustment assistance, regional assistance, and environmental compliance compensation assistance).[39] The direct payments are loosely justified on the basis that the size of the payout is tied to fixed criteria and that recipients can't affect the size of the payouts. The Framework Agreement proposes to tighten the green box criteria but does not say how. Nonetheless, the green box faces pressure from two fronts: non-trade concerns and a WTO panel dealing with US cotton programs.

The Framework Agreement advocates revising the green box criteria while taking into account non-trade concerns. Non-trade concerns cover a number of issues including food security, protection of the environment, ensuring the viability of rural areas, and animal welfare considerations. Multifunctionality is the idea that farming produces non-priced spillovers, or by-products, whose beneficial aspects are under

[38] The three countries are: the United States, the European Union and Japan.
[39] The attributes of public goods are that they are non-rival (one person's consumption does not reduce an others) and non-excludable (access can't be denied). The policy implication is that the market fails to provide an adequate amount of the good.

provided. Several Members equate non-trade concerns with multifunctionality (Paarlberg, Bredahl and Lee).

Proponents of multifunctionality argue that these spillovers have a public good aspect and that the market fails to provide an adequate amount of the public good. As a remedy to this problem, they argue that coupled production subsidies should be used to promote agricultural output and the associated benefits from the non-food spillovers.

The critics of multifunctionality counter that although these spillovers may exist they are not exclusively generated by farming and that they are also generated by other sectors of the economy. Furthermore, not all of the spillovers are positive benefits; negative spillovers from farming e.g. manure smells impose unpriced costs on society. The critics view multifunctionality as a thinly disguised attempt to circumvent the domestic support disciplines and argue that the green box can be used to promote multifunctionality.

The public good aspects of multifunctionality are very different than the public goods identified as general services in the green box. Furthermore, direct payments based on fixed criteria are not an efficient method of providing public goods. Consequently, it remains an open question whether or not there is a legitimate public goods aspect to multifunctionality. If non-trade concerns are legitimate public goods then the green box does not provide sufficient guidance on how to differentiate these programs from measures with protectionism as the primary motivation. There is little support for multifunctionality outside of Norway, Switzerland, Japan and South Korea (and to a limited extent the EU). At this stage of the negotiations non-trade concerns are not discussed as a separate item. Instead, non-trade concerns are supposed to be taken into account in the negotiations on each of the three pillars: export competition, market access and domestic support.

The second challenge to the green box comes with respect to direct payments to producers in the form of decoupled payments. A recent WTO panel on US cotton programs ruled that the US production flexibility contract payments and direct payments did not meet the green box criteria. The panel's argument was based on a technicality that the land based payments had a requirement that fruit and vegetables not be grown on this land. So the payment level does in effect depend upon the crop grown and is therefore not fixed. With minor modifications the US could fix this problem, however the challenge to the decoupled payments raises potential problems for both the EU and the US in terms of future challenges to their use of the green box. Swinbank and Tranter contend that decoupled payments are not supposed to be based on factors of production employed in any year after the base period, yet the EU single farm payments (and US direct payments) are land based. Furthermore, up to 25 percent of EU compensatory blue box payments can be retained as crop-specific area aid and not converted to the single farm payment. So, the EU would have to notify part of the former compensatory payments as green box programs and the remainder as blue box payments. Swinbank and Tranter see this interpretation as potentially open to challenge. An analogous problem would arise if Canada chooses to notify part of the payouts under CAIS (when the production margin falls by less than 30 percent of reference margin) as non-product specific AMS and the remainder (margin declines of more than 30 percent) as green box eligible.

What is the potential for new green box criteria? The EU opposes any change to the criteria and the US will likely resist changes. Consequently, major criteria modifications seem unlikely, but there will be pressure to change the green box. At a minimum, notification requirements for green box programs are likely to be strengthened, and those countries that use the green box for domestic support will be under increased scrutiny and required to justify the exemption of their programs from support reductions.

2.7 Tariff Preferences – Why They Are Important

A pillar of the WTO is nondiscrimination. Nondiscrimination means that foreign firms should be treated the same as domestic firms except for the import tariffs they face, and all foreign firms should be treated the same. However, there are many exceptions to the principle of nondiscrimination. The primary exception to nondiscrimination relates to bilateral trade agreements, free trade areas such as NAFTA and common markets such as the European Union (now containing 25 member countries). In addition, many developing countries enjoy preferential access to developed country markets based on historical relationships.

From Canada's perspective the preferential access of developing countries to developed country markets is not a large issue. Canada provides access to its market through a generalized system of preferences for developing countries. As long as nothing is done in the WTO to force Canada to open its highly protected sectors of dairy and poultry to developing country exports, Canada is likely to support initiatives that give developing countries greater market access. Conversely, tariff preferences are a huge issue for some developing countries. As tariffs are lowered developing countries that have enjoyed long standing preferential access into some developed country markets are going to see these preferences eroded. This may drive out traditional high cost developing country exporters, currently facing low tariffs, and replace them with low cost nontraditional suppliers. While this rearrangement of trade is consistent with comparative advantage, producers of some commodities in some developing countries will be harmed. As a result, these Members may find themselves opposing trade liberalization in order to protect traditional tariff preferences. It may be necessary for the rich nations of the world to provide some development assistance to poor countries that are clearly harmed by the loss of tariff preferences during the process of trade liberalization.

Canada faces its own loss of tariff preference, but it has nothing to do with the WTO or the Framework Agreement. For 15 years, Canada has had preferred access to the United States market and as shown in section 1.1 a very large proportion of Canada's trade growth has been in the United States. Recently, the United States has become very active in negotiating bilateral trade agreements with other nations. Since

NAFTA was signed the US has negotiated bilateral agreements with Jordan, Chile, Singapore, Morocco and Australia (Burfisher and Zahniser). Each bilateral accord the Unites States signs erodes some of Canada's preferred status in the United States market. Worldwide, an increasing number of bilateral trade agreements coupled with a significant number of regional trade pacts have the potential to turn the world into what Bhagwati has called a spaghetti bowl of trade arrangements. An aggressive result from the DDA would do much to slow the growth of preferential trading arrangements and open markets outside the United States for Canada's exports.

2.8 Export Taxes/Prohibitions and Restrictions

The Framework Agreement is largely silent on the issue of export taxes, export prohibitions and export restrictions except to say that the disciplines applied to these measures will be strengthened. It will not be difficult to strengthen the disciplines since all that is currently required is to take "due consideration of the effects of such prohibition or restriction on importing members' food security (Article 12 of AoA)" and to notify the Committee on Agriculture.

With the exception of the short lived Russian grain embargo in 1980 Canada has not used export prohibitions/taxes and export taxes are unconstitutional in the United States. If developed country exporters want more open markets they need to take heed of food deficit importers legitimate concerns about food security. At the very least this means importers should be assured that they will not be shut out of world markets when supplies are short and prices are high. The use of export restrictions and prohibitions should be banned for use by developed countries and allowed for developing countries only under clearly specified conditions related to food security.

Export taxes are the flip side of export subsidies.[40] If export subsidies are eliminated during the DDA then it seems reasonable to eliminate export taxes at the same time. Export taxes are usually applied to raw agricultural commodity exports to encourage domestic processing. Export taxes are a tax on domestic farmers and provide a subsidy to domestic processors. Effectively, export taxes act as another form of tariff escalation and relatively small export taxes can provide considerable effective protection for domestic processors (Houck).

Ideally, the use of export taxes will be eliminated on the same implementation schedule as export subsidies and for the same reasons. If exceptions are allowed for developing countries then differential export taxes should be banned and restrictions placed on their use by developing countries.

[40] There is one key difference between export subsidies and export taxes. An export tax generates revenue for the country using this instrument while an export subsidy requires government expenditures. A few Members might require assistance as the revenue from export taxes is lost.

2.9 Simple and not so Simple Things that Need to be Done

There are a number of initiatives that should be taken during the DDA to avoid some of the problems and inequities that plagued the UR. Some of these initiatives are relatively simple in concept but potentially dangerous in implementation. Other ideas are simple both in conception and implementation, but will meet stout challenges during the negotiations – perhaps even from Canada. However, if implemented in good faith each of theses ideas will improve the outcome of the DDA and maker future negotiations easier.

First, all complex and specific tariffs should be converted into there *ad valorem* tariff equivalents.[41] Complex and specific tariffs are common for agrifood products and they reduce the transparency of protection levels, are complex to administer and make comparisons of tariff levels across countries and products difficult.[42] However, the process of converting from specific and complex tariffs should not be used as an opportunity to raise tariff levels as was the case during the UR tariffication exercise. For this reason, the *ad valorem* tariffs that replace current specific and complex tariffs should be calculated by the WTO Secretariat or calculated by Members according to detailed rules negotiated and incorporated into the legal text of the WTO. At the very least, this requires the acceptance of a common set of indicative international prices (FAO) and the DDA tariff reductions should be taken from the newly established *ad valorem* tariff equivalents. As this paper is being written it appears a preliminary compromise on the calculation of *ad valorem* tariff equivalents has been reached but WTO Members have yet to ratify the details.

Second, minimum access commitments under tariff rate quotas should apply to a recent common base period for domestic consumption and DDA minimum access commitments should provide a meaningful level of access such as the larger of a five percentage point increase over current access or minimum access of ten percent of recent consumption.

Third, in-quota tariffs under tariff rate quotas should be cut to zero, and Members should agree to uniform rules for administering the minimum access quantities under tariff rate quotas. This should improve TRQ fill rates and remove the in-quota tariff as a protective instrument.

Fourth, there should be no exceptions to tariff cuts. It should be agreed that nuisance tariffs less than five percent will be cut to zero and that there will be a ceiling on tariffs, even if the initial ceiling is high.

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[41] Complex tariffs involve some combination of a specific (per unit) tariff and an *ad valorem* (percentage) tariff. For example, Canada's over quota tariff on cheddar cheese is complex (245.6 percent but not less than $3.528 per kilogram).

[42] Although specific tariffs may be more meaningful to those intimately engaged in the day the day minutia of trading specific commodities a percentage tariff has more meaning to those with less detailed knowledge of the sector.

Fifth, members should commit to providing timely notifications on domestic support, export competition and market access, including TRQ fill rates.

3.0 Conclusions

The Framework Agreement provides the basic building blocks on which a final Doha Development Round agreement will be constructed. Like any skeleton it does not describe the features or specifics of the final product, but it does give an indication of the basic structure. In terms of ambition, a final judgment must await agreement on the modalities but it appears that the Framework is ambitious enough to keep the process of liberalization going, but it also reflects as much concern among the negotiators with continuing protection for special interests as with promoting opportunities for healthy competition.

What does the Framework mean for Canadians? This question can be addressed from two perspectives. First, from the perspective of governments and interest groups, the negotiations have moved well past the initial negotiating position put forward by the Canadian government in 1999. The Framework is a mixture of things that reflect the government of Canada's negotiating aspirations, and liberalization that goes beyond what the Canadian government was seeking. The Framework does give the Canadian negotiators scope to continue pursuing the objectives of the official Canadian position. Second, from the perspective of ordinary Canadians a strong multilateralist agenda is more important than ever with the growing proliferation of regional trade agreements. Canada has benefited from its membership in NAFTA but stands to lose trade preferences as the US aggressively pursues bilateral trade agreements. Promotion of market opportunities for less developed countries is as important for the Canadian economy as it is for the economies of these markets. Developing countries are the future markets for both bulk and processed Canadian agrifood exports.

The Canadian negotiators were seeking an overall limit on all types of domestic support (green, blue and amber programs) and the maximum possible reduction in amber and blue box support. The Framework will discipline the total amount of AMS, blue box, and *de minimis* support. This is potentially one of the most significant contributions of the Framework Agreement. A discipline on overall spending that includes the green box would violate the principle of redirecting support through less trade distorting avenues. The harmonization approach will be more aggressive in reducing subsidies in those countries that subsidize the most. Product specific caps on amber box support will prevent Members from continuing to provide trade distorting domestic support to selected sectors, as overall support levels are reduced. This may limit future increases in support prices for Canadian dairy products, but the discipline should be useful if the total AMS reduction commitments are binding for large agricultural subsidizers. At this time it is not known how large the required reduction in *de minimis* support will be, but a smaller threshold may create a challenge for Canada in terms of meeting its domestic support commitments.

Canadian negotiators were looking for the elimination of all agricultural export subsidies as quickly as possible. The Framework will eventually eliminate direct export subsidies but this is unlikely to happen before 2015. Disciplines on government involvement in agricultural export credit programs are long awaited and should help to bring agriculture closer to the set of subsidy disciplines that apply to other sectors. Any discomfort that these disciplines might create for the CWB should be far less than the benefit of knowing that the US will have less opportunity to promote its exports by offering export financing conditions that are better than those offered in a competitive market. This will require the CWB to develop innovative risk management techniques to underpin its initial payments. Furthermore, the CWB will need to increase its asset base in order to be able to establish a solid credit rating and to lower its borrowing costs.

Canada was seeking a variety of market access negotiating techniques that would open foreign markets to the greatest possible extent while still protecting sensitive domestic industries. The Framework introduces a category of sensitive products. Market access liberalization for sensitive products will be made through a combination of tariff reductions and tariff rate quota expansion. It is not, however, in Canada's interest that a plethora of exemptions be created with respect to market access commitments. The Canadian negotiators hesitancy to lower over-quota tariffs is not realistic as cuts in all tariffs are to be expected. The Canadian negotiators were seeking a minimum access commitment equal to at least five percent of current consumption of the product concerned. Hopefully the negotiators will be more successful in opening markets than this modest objective suggests. Consumers and purchasers of intermediate inputs will all benefit, but trade also exposes domestic producers to increased competition requiring them to be more efficient and to produce better products. It is important that the base for tariff quota expansion be established through coherent and equitable criteria, and that Members be discouraged from ignoring this criteria in their final offers. Reducing the dispersion of tariffs and their escalation is a goal that Canadian negotiators should be seeking given the proportion of our exports that are consumer ready.

While Canada was willing to discuss practical trade concerns about the activities of single-desk exporters of agricultural products, it would appear that of the 148 WTO Members only a few support Canada's position on STEs. In our view, questions of addressing the market power of STEs and of transnational corporations are best dealt with in the arena of international competition policy. However, this is a question that was deferred to future negotiations. Canada may have to accept some discipline on the actions of single desk STEs, but the negotiators are still arguing from a strong position that disciplines for developed country agricultural exporting STEs should not be significantly different from the disciplines applied to all other STEs.

The next touchstone for the DDA negotiations is the end of July 2005 when negotiators are expected to provide a “first approximation” of an eventual agricultural deal. However, as stressed in this report a number of difficult issues still confront the negotiators, especially with respect to market access. Mr. Tim Goser who heads the Committee on Agriculture has indicated he doesn’t expect a decision on a tariff reduction formula until the Hong Kong Ministerial in December 2005.

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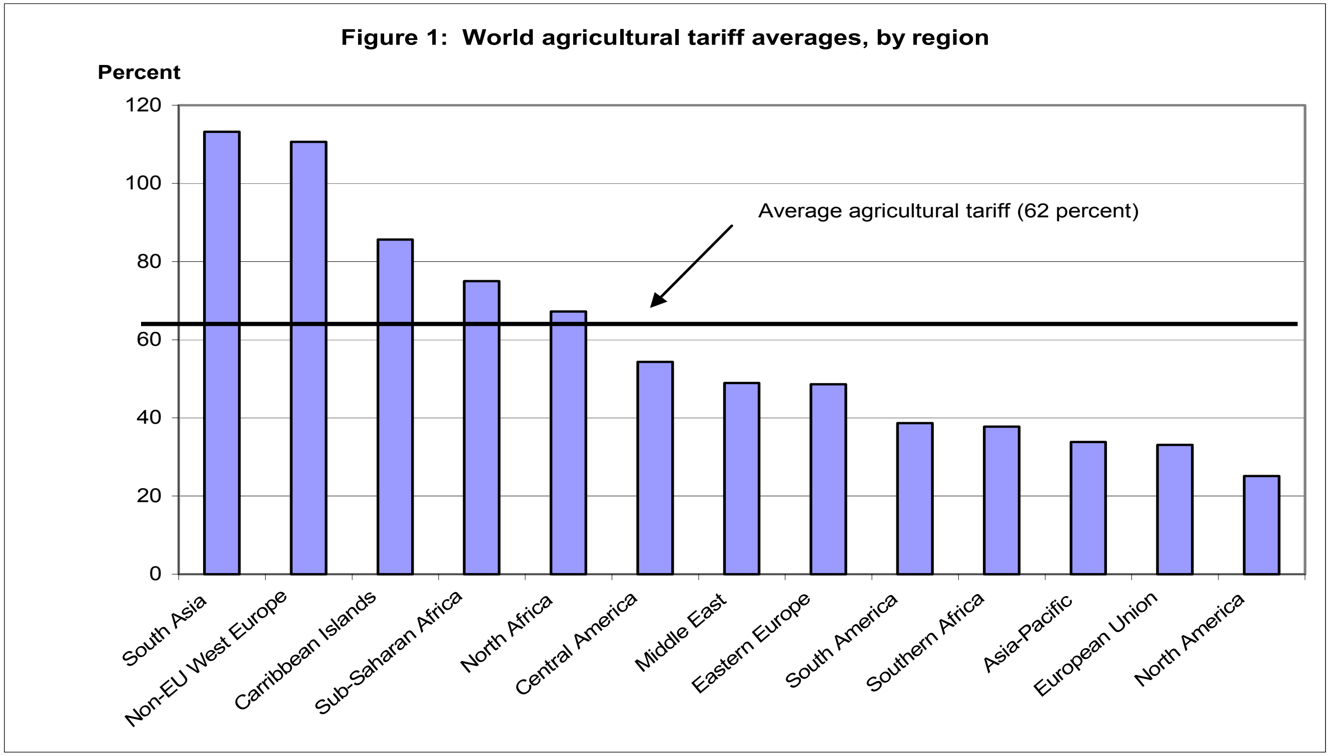
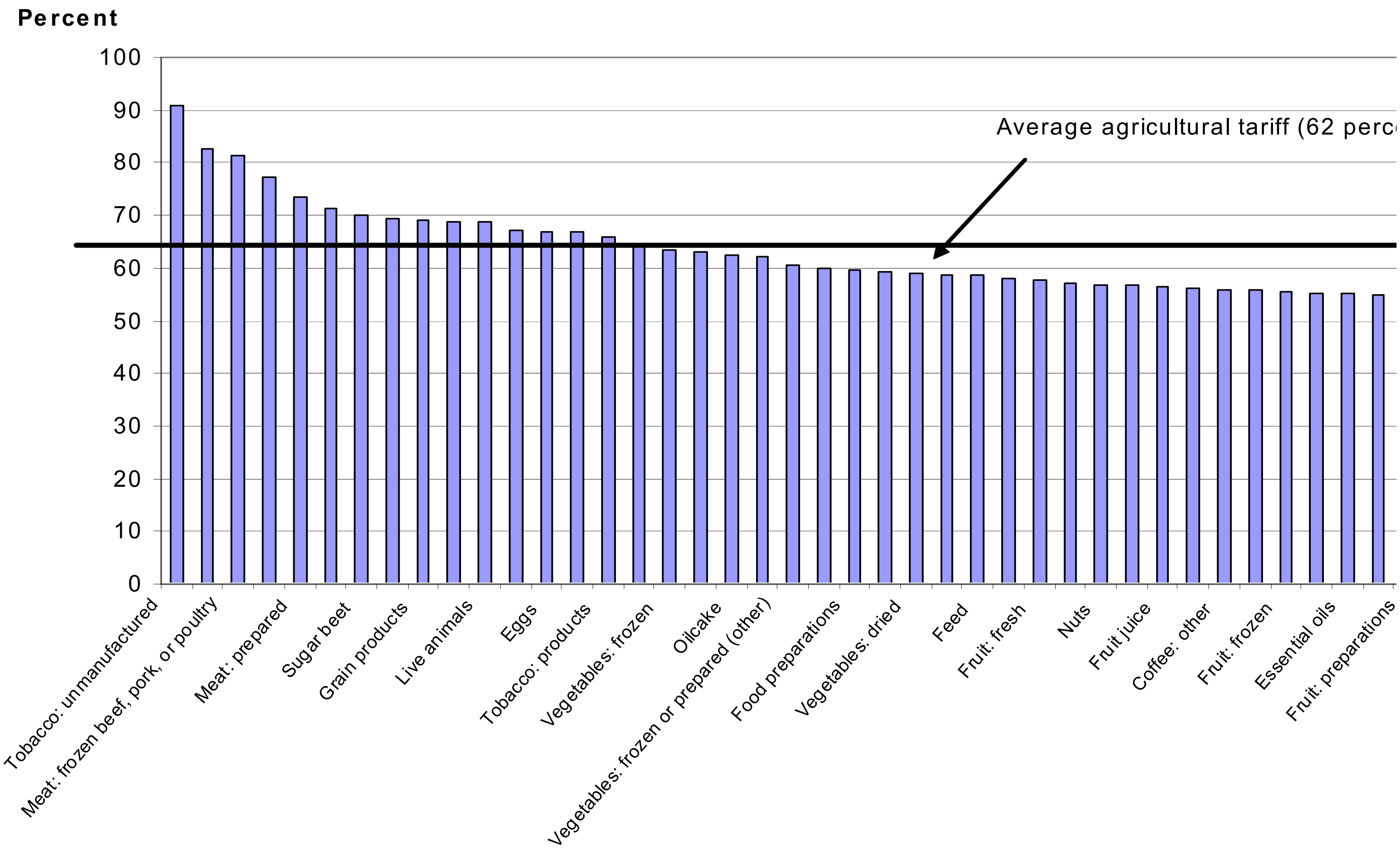


Source: Gibson, Waino, Whitley and Bohman (2001)

Figure 2: World agricultural tariff averages, by commodity



Source: Gibson, Waino, Whitley and Bohman (2001)