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The WTO and Farm Policy in the United States: Implications from Agreements, Dispute Settlement, and Current Negotiation

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Slide 1



**The WTO and Farm Policy in the United States:
Implications from Agreements, Dispute
Settlement and Current Negotiations**

**Presented at the workshop on
Political Economy of Agri-Environmental Policies
in the U.S. and the EU
Grass Valley, California
May 28, 2005**

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Outline role of WTO in domestic farm policy

- **Three linkages**
 1. **Adjust programs to comply with past agreements**
 2. **Respond to dispute settlement with policy changes**
 3. **Anticipate new WTO agreements from negotiations and interact policy planning with negotiations**

**WTO in Geneva influences US policy and
the US influences the WTO**

**For farm groups and others in the US the
WTO seems foreign, but it remains heavily
influenced by US practices and procedures**



Role of WTO

- **The WTO is a club organized and run by member governments to liberalize trade.**
- **The WTO plays two roles**
 - **Supervise implementation of agreements including settling disputes among members**
 - **Provide the framework for negotiating new agreements**
- **US disputes settled in March include cotton subsidy dispute won by Brazil, and EU geographic indicator dispute won by the US.**
- **The Doha Development Agenda is also at a critical juncture.**

Role of WTO in trade policy

WTO and the GATT have been the international vehicles for coordinated trade-related policy changes

Many trade policy studies ask how multilateral changes in barriers and subsidies affect markets, often in the context of a stylized negotiated agreement

Much less examination of the WTO role in dispute settlement

Many view the WTO as a monster



**Is the WTO a
toothless poodle
or a
uncontrollable
fire breathing
dragon?**

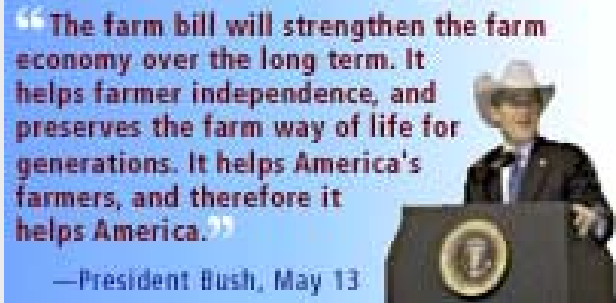
**Actually...neither
The WTO is a
modest tool to
facilitate
reductions in
trade barriers
and trade
frictions.**

From the WTO website:

“The WTO is the only international body dealing with the rules of trade between nations. At its heart are the WTO agreements, the legal ground-rules for international commerce and for trade policy. The agreements have three main objectives: to help trade flow as freely as possible, to achieve further liberalization gradually through negotiation, and to set up an impartial means of settling disputes.”

Commodity subsidies affect production and affect environmental outcome

- **President Bush praised “The Farm Security and Rural Investment Act of 2002”**



Periodic U.S. farm bills are large and complex

- **Hundreds of pages: \$\$\$ for food stamps, rural telephones, R&D, foreign food aid, and more**
- **Main focus is big \$\$\$ for subsidy for grains, oilseeds, and cotton (subsidy averages 20% of revenue, but 40% or more for rice and cotton)**
- **Other payments, regulations or trade barriers subsidize dairy, sugar, and others**
- **Most commodities get little subsidy (for example, this includes 70% of California agriculture)**
- **Environmental subsidies and compliance rules are may affect production and trade**

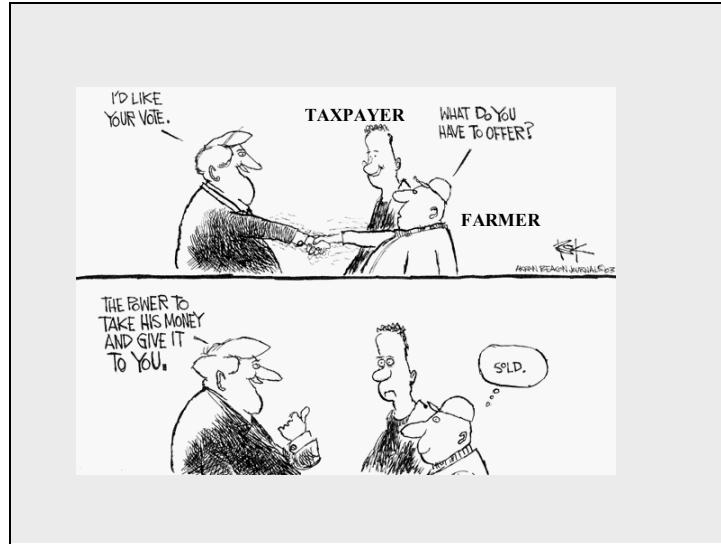
Budget projections for farm subsidies (\$Billions)

	FY 04/05	FY 05/06
Feed grains	8.2	8.6
Soybeans	2.1	2.2
Wheat	1.6	2.2
Cotton	3.3	2.5
Rice	0.6	0.9
Dairy	0.8	0.3
Other commodity	0.5	0.6
Disaster	2.6	0.3
Other	1.0	1.0
Total	\$20.7 Bil	\$18.6 Bil

A political economy model

Need a model to explain the pattern of wealth transfer to farmers and other favored groups.

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Slide 13



The WTO cotton dispute overview

- **The cotton dispute dealt with:**
 - (1) use of “prohibited” subsidies that the US had pledged not to use, and
 - (2) “serious prejudice” meaning the overall effect of the package of subsidies caused the price received by Brazilian farmers to be below what it would otherwise have been.
- **Prior issue, Brazil had to show support in 1999-2002 exceeded support in 1992 (Peace Clause)**
- **Judges were three “panelists”: a former finance official from Poland, a private trade lawyer from Australia and a trade negotiator from Chile.**
- **The U.S. had to defend its programs not as good policy or “fair”, but only as not inconsistent with the WTO agreements that the US had signed.**

The Peace Clause

- **Economic and legal issues:**
- **What is “support” to a specific commodity and how is it measured?**
 - This was needed to be able to know if support had risen.
- **Brazil argued budget outlays**
- **US countered with rate of price support**
- **US wanted to leave aside many programs as non-trade distorting or not specific to cotton**
- **The bottom line was a tightening of green box rules that seem to lower the threshold for “minimally trade distorting” relative to what the US has assumed**
- **Implications for enviro programs wanting to be green?**

Main WTO cotton dispute issues

Brazil claimed:

1. Step 2 domestic payments are prohibited domestic content subsidies
2. Step 2 export payments are prohibited export subsidies
3. Export credit guarantees are prohibited export subsidies
4. flexibility contract payments and direct payments, market loss assistance payments and countercyclical payments, and the marketing loan gains all subsidize cotton and cause world cotton prices to be lower than otherwise and caused U.S. world market share rise
5. crop insurance subsidizes cotton and affect world market prices and share

Brazil claimed that the U.S. programs had these effects over the 1999 to 2002 period and threatened to have these effects into the future

The US lost on all major counts

- **WTO panel ruled mainly for Brazil**
(released June public Sept 2004)
 - Peace clause violated ...US “decoupled” programs not green
 - Demand subsidies ruled out of compliance ... Step 2 and export guarantees to be removed very soon
 - Subsidies caused serious prejudice by suppressing world price (not direct payment or crop insurance).
- **Appellate Body Session Decision March 03, 2005 ...**
 - Agreed with panel ... US lost every major issue

WTO Implications of the case

- **Affect the conduct of negotiations more attention to specific wording.**
- **Pressure for rules that can be binding and predictably so.**
- **Credibility of WTO in developing countries increased significantly**
- **Could lead to more similar cases, but these are hard to develop**
- **Implications for the role of economists**
 - **Far more economic argument and evidence than any other and certainly more than other agricultural disputes**

Implications for US farm programs

The US Congress and farm groups are angry at the WTO and express much outrage at WTO interference.

Green box findings mean programs must be more pure

Domestic content finding may affect price support, government purchase programs (dairy)

Export credits must be reformed sooner than DDA

Affects on world markets will be hard to demonstrate generally, but some commodities are concerned

- **Overall US farm subsidies are not the major driver of producer welfare in other countries. This has been over-sold in the media and by NGOs.**

These implications could apply to the EU and others.

DDA negotiations and US Farm Policy

- **Outline of DDA agriculture agreement is clear from the August Framework agreement.**
 - Access to expand substantially, but less for special and sensitive products ... rice in Korea, in US sugar, dairy?
 - Export subsidies including credit subsidy, STE subsidy and commercial substitute food aid will be eliminated.
 - Domestic support rules will tighten, and subsidy reduced, but new blue box will allow smaller cuts for 'almost' green-box programs.
- **DDA is scheduled to arrive at modalities by December 2005**
- **The schedule may slip, but expect agreements in 2006 with implementation in 2007 or beginning of 2008.**
- **This schedule fits nicely with US farm bill schedule to be settled in early 2007 for 2007 crop years.**
- **Also fits with implementation of cotton dispute results.**

New farm bill due in 2007

Preparation is underway now.

- **Commodity groups are lining up support and others are readying positions analysis**
 - Last week at the Davis International House one of a set of regional sessions on planning for the next farm bill sponsored by the American Farmland Trust (a Washington DC lobby group and farm land preservation actor).

Their focus is on how to shift \$\$\$ from commodity subsidy to environmental benefits and perhaps public research

They use the Doha negotiations and the cotton decision as a motivator and rationale

But are the environmental programs contemplated consistent with WTO obligations?

Working land payments basics

- **There are few economic incentives for growers to use additional conservation or “stewardship” practices that mitigate negative environmental externalities or provide positive environmental amenities.**
- **Policy incentives have relatively little funding.**
 - **Traditional environmental enforcement provides negative incentives by demanding compliance with penalties**
- **Stewardship payment programs can offer rewards to farmers to use listed “green” practices.**
- **The idea is to provide support to farmers while helping the environment.**
- **Added incentive if these are WTO green**
- **Added incentive if these have more political support**

Two approaches to working lands payments

A. Reward farmers for current green practices

Does not improve environment

Recognizes good practices now undertaken

Net gain to farmers

Fair to farms that are already more eco-friendly

B. Reward farmers only for new green practices

Creates incentives for environmental gains

Limited net benefit to growers

Relative penalty for those already green

Farmers & Environmentalists should fight over A versus B

**Money allocated for “approved”
current practices**

**Such payments provide higher revenue per acre for few
if any additional costs for many growers**

- **More land will be planted,**
- **Prices will be lower,**
- **Budget costs for marketing loans and other counter-cyclical payments will rise**
- **Actual cost of the program will be larger than the payments themselves**
- **Farm benefits will be smaller, and negative for non-participants**

Working lands payments are obviously production enhancing. Will they be WTO Amber?

They also represent an increase of subsidy for “non-program” crops with little subsidy now. They could cause commodities to exceed minimal limits and be counted in AMS

Also have negotiating implications in dealing with other countries with less subsidized commodities

US farm policy changes on the horizon

Three drivers are pushing major changes in US farm subsidy program...budget deficit, WTO cotton dispute, WTO-DDA negotiations.

Also, sympathy for farmers is limited... they are just one more powerful group wanting more money

Some changes will occur before the next farm bill and before DDA agreement.

Other changes will implement the DDA and the cotton dispute implementation with the new farm bill.

Just my assessment. I may be wrong!

**WTO agreement will tighten rules and
reduce farm subsidies**

**WTO and other forces will likely lead to smaller
subsidies and less influence of subsidies on trade**

- **Such changes will comply with cotton WTO result,
lower the budget costs and allow more market
opening overseas**
- **Major subsidies will remain, especially crop
insurance and “almost green box” payments for
cotton, rice and others**
- **Some increase in subsidy for environmentally
friendly practices, but these may not be green box.**
- **A WTO dispute may be needed or this could be
settled with explicit rules on boxes.**