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Red, Green, Blue or Amber: A dollar is a dollar (Towards better balanced Agricultural trade rules)

Notes for a Presentation
by

Peter Clark
President

Grey, Clark, Shih and Associates, Limited

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Since the mini-ministerial meeting in Montreal it has become increasingly clear that if the WTO rules continue to ignore the serious disruptive effects of all domestic support paid by wealthy countries Cancun, like Seattle, could crash and burn, in the process risking the entire Doha Development Agenda. Without an agreement on agriculture there will be no deal which will come even close to achieving the ambitious goals set at Doha less than two years ago.

Few, if any, are satisfied with the results of Agricultural negotiations. True, there have been relatively few disputes on agricultural products, in large part because of the Peace clause – may it die a quick and painless death – but those we have seen, including *beef hormones*, *bananas* and *dairy products* are important. (I leave aside safeguards and other “unfair trade” issues involving lamb, HFCS.)

Developing countries are concerned because they have not received expected market access for their products. Their home markets have become dumping grounds for excess production from developed countries where generous subsidies, though not explicitly tied to exports, stimulate surplus production which can only find customers in export markets. Often those exports are priced well below cost of production.

The use of domestic support continues to be a significant problem. There are charges and countercharges that supposedly “green box” support is, in fact, trade distorting. Producers in developing countries continue to suffer because they are

forced to compete with agricultural goods produced with the assistance of “green” support granted by developed countries.

It does seem clear that the very deep pockets approach of the U.S. Congress continues to disrupt markets and depress prices for a wide range of commodities. In the most heavily subsidized areas, production has expanded, creating gluts on world markets. The United States has not only increased the amount of support provided under the Farm Bill, but that support is concentrated so that it benefits a select group of largely export-oriented commodities, like corn, wheat, and soybeans.

It is because of these subsidies that poor Mexican farmers are being devastated. They blame NAFTA but the real problem is that the WTO imposes no discipline whatsoever on subsidies a Member chooses to present as “green”. Unless they are challenged, and they must be challenged as the WTO is not a self policing organization, there will be no disciplines on these “green” subsidies.

Dispute settlement has also changed the nature of the rights and obligations in the Agreement. The negotiators must take these changes into consideration and understand their impact.

Members need more time for much needed reflection. Is it time for governments to adopt a new approach to multilateral negotiations on Agriculture? Is there an adequate understanding of where we are, how we got there and where we should be going? The WTO process reflects an abundance of conventional wisdom, and traditional positioning. To what end? Repetition of polarized positions means

becoming more entrenched and an increased risk of failure, however we might define failure after this week.

Should governments be making haste slowly, taking care of unfinished business? Would it be prudent to catch up with evolution of the rules under the Agreement on Agriculture – and to take a fresh and critical look at the negotiating process?. Is it necessary to ask some tough questions about whether the Uruguay Round approach, or the use of so-called universal modalities to liberalize trade in non-agricultural goods, is the best approach for agricultural trade.

How should WTO Members respond to these changes? Is it time for Members to more actively pursue dispute settlement to preserve their rights and to ensure that they do not pay for the same fish twice in the negotiations?

The most important question is how WTO members can hope to further liberalize agricultural trade unless they face up to the extreme disruption of so called “green” subsidies. This clearly is the central issue for developing countries.

The key issues are how to define non-distorting and how to ensure that deep pockets do not permit some members to seize advantages which they would not enjoy absent such generous financial support.

Since the mid-1980s we have monitored and analyzed financial support to Agriculture in a number of countries including the USA. We found generally that U.S. support has been increasing, not declining as one would have expected after the Uruguay Round. The Wall Street Journal of June 16, 2003 reported that this

year USDA is predicting that federal subsidy cheques to U.S. farmers will double to \$21.4 billion because of the Farm Bill and will contribute to a 53% increase in farm incomes over 2002. Several years ago, the New York Times reported that subsidies to North Dakota farmers have exceeded net farm income.

In a recent report, we examined the financial assistance and subsidy programs of a number of countries including the USA and New Zealand to determine how the new interpretations since the end of the Uruguay Round might impact on the existing programs of major trading countries.

This report concludes that:

- the USA provides domestic support and export subsidies to its agricultural producers in excess of its bound WTO commitment levels; and
- New Zealand, through Fonterra, provides export subsidies to support, promote and enhance its exports of dairy products.

New Zealand has permitted, indeed has legislated, the establishment of Fonterra Cooperative Group, a highly monopolistic merger exempt from the disciplines of Competition Policy. Fonterra has captured virtually all of New Zealand's dairy production and has been granted the exclusive right to export dairy products to high-value markets, which permits it to earn profits enabling it to sell into lower-priced markets (at less than industry-wide average costs of production).

The European Union has also raised concerns about Fonterra. An August 20, 2003 Article in the New Zealand Herald, *EU fires shot at Fonterra*, reports that,

“the EU has repeatedly claimed that Fonterra’s legislated stranglehold on dairy quotas through 2007 for the EU and US markets makes it a *de facto* single-desk seller.”

The Article also points out the E.U. concern that Fonterra uses its status as a single-desk seller to offer lower prices on exports into some market, thereby providing export subsidies.

The USA exceeds its \$19.1 billion commitment by improperly classifying support as “green” or *de minimis* and by failing to include substantial, indeed massive, domestic support programs in its AMS, such as the water that it provides for irrigation.

The U.S. exceeds its export subsidy commitments through uncounted export credit guarantees, California’s administered dairy pricing system, massive domestic support that encourages surplus production that must be sold on the export market and through Article 9.1(c) export subsidies (export sales at below total average cost of production that are financed by the domestic support programs).

Cash is fungible – that is, money is money – and the U.S. has ensured that their farmers get it no matter how it is dressed up or squeezed through apparent loopholes.

Who suffers? Many smaller less affluent countries and developing countries suffer most. Why? Because this is not a game of right and wrong – it is a game of big and little. Most countries have met their obligations on both domestic and export support. They can't afford not to. Canada and Mexico are next door to the USA – and have integrated markets with them for many products because of NAFTA. The principal difference is that Canadian and Mexican farmers' income must come from the market, while much of the American farmers' will come from the U.S. Treasury.

Our conclusions were thoroughly analyzed and documented. The report highlights the fact that some WTO Members are not living up to their WTO obligations. It also explains how WTO obligations have been changed through Dispute Settlement. There are many other examples of programs adopted in good faith in the belief that they were not subsidies, or that they were not subject to AMS or export subsidy commitments, that will now violate WTO obligations.

The E.U.-USA framework will not solve the problem. It is far too self serving and if it were negotiable, it would exacerbate the problems of smaller countries.

The E.U. for a variety of reasons is embarking on a reform of the CAP. The USA and other export-oriented countries consider it is not enough. But E.U. Trade Commissioner Pascal Lamy points out it will be easier to reach a meaningful agreement if the principal parties adopt realistic approaches and abandon their philosophical/theological crusades for totally open markets. Europeans and many others will not impair their ability to feed themselves.

Since the Uruguay Round results were adopted in 1994, and particularly over the last 5 years, it has become apparent that the WTO has evolved in ways which differ significantly from expectations. These differences, how they occurred and their implications for WTO Member Countries are particularly important issues to be addressed this week

Concerns about the WTO dispute settlement process are not limited to Agriculture. John Magnus, in a recent presentation to the Canadian Bar Association, said that decisions by the Dispute Settlement Body have “minted and imposed new obligations” on WTO Members.¹ Mr. Magnus referred to the changes wrought by these decisions as “mission creep”.²

Alan Wolff, former Deputy US Trade Representative and USTR General Counsel has also raised concerns noting that,

“... dispute settlement panels are acting outside their authority and are in effect re-writing the WTO agreements contrary to international law as well as the intent of the parties to the WTO.”³

There are important differences between dispute settlement in the GATT and WTO. Dispute settlement is no longer an exercise in diplomacy based on conciliation. The system changed and become politicized.

¹ John Magnus, *Recent WTO Cases Involving Trade Remedy Measures: Flawed Decisions Emerging from a Flawed System*, Presentation at the Canadian Bar Association’s Fourth Annual International Law CLE Conference, Ottawa, Ontario, June 6, 2003, at page 1.

² John Magnus, *Recent WTO Cases Involving Trade Remedy Measures: Flawed Decisions Emerging from a Flawed System*, Presentation at the Canadian Bar Association’s Fourth Annual International Law CLE Conference, Ottawa, Ontario, June 6, 2003, at page 2.

³ Alan Wm. Wolff, *Major Problems with WTO Dispute Settlement*, Remarks made at the Global Business Dialogue, Inc., Washington, D.C., September 26, 2002, at page 2.

The impact of the disputes has also changed. WTO disputes may deal with specific issues between specific Members, but the decisions potentially affect all Members. The condemnations issued by the Dispute Settlement Body do not automatically extend to similar practices and policies employed by Members not the subject of a particular challenge. The WTO is not self-enforcing. Challenges are essential in order to maintain balance. To ignore this exacerbates imbalances.

The changes in dispute settlement have far-reaching implications for negotiators and for their expectations. The trade negotiator or trade policy specialist understands that the WTO agreements, which are negotiated among more than 140 countries of widely differing expertise and experience, are not the same as a contract for mangoes or semi-conductors negotiated between a few knowledgeable participants. The WTO agreements are, because of the nature of the process, less precise - they paper over differences in views and expectations. Yet in dispute settlement, the words have only their plain meanings and differing expectations are ignored.

Trade negotiators and policy officials may understand that trade agreements are about compromise and that each issue is part of a bigger puzzle. It is important that the Party making concessions be permitted to do so with its honour intact, and most important, be permitted to save face, and I must add, as well as looking after their essential national interests.

This approach was best explained, in my view, by the first Executive Secretary of the GATT, Sir Eric Wyndham-White. Sir Eric said that the best type of agreement or solution was one which was mutually unsatisfactory.

But, the changes in the dispute settlement system and its impact on the obligations in the Agreement must be taken into consideration by negotiators. The unintended result of the more legalized and litigious WTO Dispute settlement process – at least unintended by most – is that Dispute Settlement Panels have interpreted the WTO Agreements in ways which created new obligations, modifying what some countries considered they had negotiated.

The Uruguay Round rules have changed, and changed in unexpected ways. The WTO Panel in *Canada Dairy*, confirmed by the Appellate Body, has severely limited Canada's ability to export dairy products without being deemed to be conferring export subsidies. More change may be coming from the various other challenges including Thailand's challenge of certain aspects of the EU sugar regime.

The Panel and Appellate Body considered Article 9.1(c) of the Agreement on Agriculture, which deems that a payment made on the export of agricultural products that is financed by virtue of governmental action is an export subsidy. They found that government finances a payment if it transfers economic resources that *enable* a third party to make a payment.

There is no need for government to require that the payment be made. There is no need for the government to even be aware that the third party is making a payment

because of its financing. There is no need for the financing measure to be WTO-inconsistent or to be directed at exports. The government measure simply has to exist. There is also no need for the payment to confer a benefit on the recipient.

This means that government may not have a role in the export subsidy and no control over when the export subsidy is given. Governments may have no ability to determine whether or not it is giving export support within its bound limits. Government is virtually taken out of the process. The negotiators could not have intended this result.

The Appellate Body arguably went beyond its jurisdiction in issuing its Report in *Canada Dairy*. Articles 3(2) and 19(2) of the Dispute Settlement Understanding limit the Appellate Body by prohibiting it from issuing recommendations that add to or diminish the rights and obligations of the covered agreements. The Appellate Body can clarify, but it can go no further.

Unless the Appellate Body is restrained and restricted to clarifications that do not change the nature of the Agreement, we will be confronted with more Reports that change the nature of the Agreement. We were aware throughout the *Canada Dairy* process that even the initial Panel report had adverse implications for a number of U.S. programs and the New Zealand Dairy Board – which has since been transformed into the Fonterra Co-op, an organization which has the same WTO conformity problems.

Thailand, Australia and Brazil have now employed the principles of *Canada Dairy* to challenge aspects of the E.U. Sugar program. The E.U., in response, suggests

that based on this approach any country benefiting from TRQs, cannot export without the benefit of export subsidies.

Should WTO Members take the time to reflect on these issues before moving ahead? There is nothing magic or crucial about the Doha objective of establishing modalities by March 31, 2003, and submitting draft schedules at the Fifth Ministerial here at Cancun. These goals were set at a meeting characterized by a need to demonstrate solidarity after the horrendous events two years ago today. They were and are like dates set in previous Rounds targets. The deadlines established at Doha were over-optimistic and never had a realistic prospect for attainment. One need only watch the rush to reduce expectations to drive this point home.

Ministers cannot say these dates are anything less than cast in stone until they are missed or it is clear they will be missed. These targets dates have often been missed in the past. For Agriculture, in the current context, this was inevitable because of:

- very entrenched differences in philosophy;
- differing agricultural structures;
- politicization of issues which ignores the realities of differences in structure, philosophy and approach to Farm policies

It is also not clear that the negotiators fully realized the impact of dispute settlement on the WTO when they set these goals. Negotiators have to take the affect of dispute settlement into consideration as they move forward and ensure

that the process gives them sufficient time to fully understand the Agreement that they negotiated.

George Yeo, the facilitator on Agriculture, a veteran of these wars indicated that WTO members need to adopt new, less ambitious approaches to avoid Cancun becoming another Seattle. More realistic expectations as envisaged by Mr. Yeo, is a recommendation shared by Pascal Lamy.

Mr. Yeo has pointed out – something which should be blindingly obvious – that agricultural reform is politically difficult for many WTO members, including Japan, Korea and China, whose ruling parties came to power with the support of the rural population. As Mr. Yeo explained,

“The problem is, in many countries, agriculture is organically wedded to the political system.”

This is true as well in Europe – and nowhere is it more true than in the USA, where notwithstanding ambitious undertakings to reduce farm financial support, expenditures keep rising – at the same time U.S. negotiators press for deeper cuts for certain subsidies and improved market access while defending their “Green Box” with extreme vigour.

Farm Bills and their generous financial support are not likely to disappear in the USA. It is apparently not what you do – it is the way that you do it, and as Washington has shown us, how deep their pockets are.

At the end of the day, pragmatism will win out over theology. But the crusaders will continue to press to ensure that at the 11th hour they have extracted all they can. This is how negotiations work.

In analyzing how we move forward, it is important to consider how long it has taken since the beginning of multilateral negotiations under GATT (1947) to reach the level of liberalization the international trading system has achieved on non-agricultural products. It has been claimed that Agriculture was largely outside the GATT until 1994. Strictly speaking, this is an overstatement, but not a great one. Are we trying to move too far too fast? Certainly the E.U. and George Yeo think this is a risk.

The other issue which should be the subject of intensive reflection and debate is whether or not it is necessary or appropriate in the Agriculture negotiations to adopt quantitative “across the board” approaches to liberalization. This was attempted in the Uruguay Round with very mixed results; results which, with the benefit of hindsight, have been particularly adverse for developing countries. The Uruguay Round liberalization was important, both as a start to bringing Agriculture into the WTO system and the absolute magnitudes in the context of existing access levels and the more water-tight protection afforded by quantitative restrictions.

There is ample evidence that these results did not generate uniform benefits for all participants. Indeed, some were worse off as they opened their markets and major players tweaked the system and exploited apparent loopholes to maintain or

increase financial support to their own producers, further distorting production and markets and depressing prices in the process.

This situation underlines the need for a fresh, zero-based approach to negotiations. Balance was not achieved in the past through a single undertaking “one size fits all” approach. The WTO agreements are not negotiated among equals. There is a need to adopt a more qualitative approach which takes account of the differences in costs, structures and social and economic development policies of individual countries. There was a request and offer process used in a GATT until the Kennedy Round. It worked well in the first 15-20 years of liberalization of non-agricultural trade. The request and offer approach seems to be working well in the WTO Services negotiations. The principal benefit of universally applied formulae is that it reduces the complexity of the negotiating process; it makes life easier for the negotiators.

Farmers around the world need farmer-friendly trade policies and negotiations based on the facts and details of their unique situations. It is better to do a proper job which reflects facts than to press ahead with “cookie-cutter” formulas which are applied notwithstanding facts or reality and for those countries with fewer resources – without proper analysis of the implications.

The natural inclination of those who would prefer to input data rather than rely on negotiating skills is to choose the universal modalities approach. They cannot handle, or will not handle the detail necessary to provide proper information to their negotiators; information which will reflect the realities of national interests. This is a system which benefits the largest players and will continue to widen gaps

between haves and have-nots. This is far too important an issue to permit an approach to prevail on grounds of simplicity.

Obviously, international rules haven't protected many smaller WTO members as they should have because the WTO rules are out of balance. The negotiators have to take steps to bring the WTO back into balance. This can't be done through a simple quantitative approach to negotiations. The negotiators must adopt a much more focused, qualitative approach to the negotiations and take the time to get it right.

The most important objective of the negotiations should be to get the right agreement, not a fast agreement. The negotiators must take the time to understand the Agreement they are negotiating and to make certain that everyone benefits.

The negotiators must also take the time to understand the impact of dispute settlement on the Agreement. The WTO is a negotiated balance of rights and obligations that has been knocked out of balance by the dispute settlement system. The negotiators have to take back their agreement.

If the negotiators are not willing to take on the dispute settlement system, then the Members will be forced to live with the consequences. To get the full benefit of WTO Membership, and to ensure that we don't risk paying for the same fish twice, all WTO-inconsistent practices must be challenged.