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CANADIAN EGG, DAIRY AND POULTRY FARMERS'

DISCUSSION PAPERS[1]

- **Inter-linkages between the Three Pillars at the WTO**
- **Market Access Package**
- **Special Agricultural Safeguard (SSG)**
- **Tariff Rate Quota (TRQ) Administration**
- **Selection and Treatment of Sensitive Products**
- **Domestic Support**

MAY 2005

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Discussion Paper[1]
May 2005

Inter-linkages between the Three Pillars at the WTO

The recognition by WTO members that inter-linkages exist between the three pillars at the WTO is an important statement and recognizes that commitments in the area of market access, for example, cannot be undertaken in isolation from the other pillars.

Prices of agricultural products in a country can remain more competitive when producers' income is supplemented by direct governmental payments, and, under such circumstances, the country has more flexibility to reduce its tariffs or pursue a policy aiming at harmonizing tariffs.

Several conditions are essential for a fair, equitable, and balanced trade agreement in agriculture to be achieved in this Round of negotiations. One fundamental condition is that, when addressing agricultural issues, it must be recognized that inter-linkages exist between the three pillars at the WTO (market access, domestic support, export competition). Fortunately, this is recognized in the Framework Agreement which states: "The reforms in all three pillars form an interconnected whole and must be approached in a balanced and equitable manner." The new rules, therefore, must account for the interdependence between policy instruments.

Market access has been traditionally defined as a tariff issue. It should be recognized that market access issues also include the abusive use of sanitary and phytosanitary measures and technical barriers to trade, but most importantly the protection provided through direct payments. Direct payments, whether amber, blue or green, restrict lower price imports from entering a given market by artificially lowering the price of domestically produced goods. To achieve equity and balance in these negotiations, the impact that direct payments have in terms of providing certain countries with flexibility on tariff reductions that other countries do not have must be taken into consideration in comparing the levels of tariffs that are maintained by different countries.

The inter-linkages that exist between the three pillars make comparisons between countries extremely challenging. Looking at tariff lines in isolation can be misleading with regards to the effective level of protection provided to a given product or sector.

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An example drawn from the United States dairy industry is used to demonstrate the implications of these inter-linkages. As illustrated in table 1, the situation would look much different if US dairy producer returns were coming solely from the marketplace. Based on preliminary results of a study by Grey, Clark and Shih and Associates Inc, the amount in subsidies that US producers receive through direct payments is estimated to be $US 2.00 per kg for butter [2]. The question then becomes, what would be the additional tariff needed if farmers were to receive all their returns from the market? The answer is depicted in Table 1.

Table 1
Estimated ad valorem tariff equivalent of payments received by US dairy producers

U.S. Butter		*Level of Protection in ad valorem* terms	
	US$/kg	Assuming a world price of 1 US$/kg August 2002	Assuming a world price of 2 US$/kg January 2005
US Tariff	1.54	154%	77%
Estimated direct payments	2.00	200%	100%
Equivalent tariff required if protection based only on tariffs	3.24	354%	177%

Source: Grey, Clark and Shih and Associates Inc.

As illustrated in table 1, an additional tariff of between 100% and 200% for butter would be required to achieve a level of border protection that would allow US producers to obtain 100% of their returns from the market place rather than through subsidies. By adding the protection conferred through direct payments, the US dairy sector is in fact protected, in *ad valorem* terms, at levels between 177% and 354%.

Tables 2 and 3 are additional examples of the limitations inherent in making straight tariff comparisons between countries without taking into consideration the protection afforded these countries through direct payments.

[2] The amount of $US 2.00 is based on preliminary findings by Grey, Clark & Shih that estimate American dairy producers received the equivalent of $US 6.41/cwt from federal programs and federal-state shared programs in 2003 and $US1.90/cwt from state programs.

Table 2 **Estimated ad valorem tariff equivalent of payments received by US cotton producers**			
U.S. Cotton		*Level of Protection in ad valorem* terms	
	US$ / tonne	Assuming a world price of 900 US$/tonne 2001/2002	Assuming a world price of 1300 US$/tonne 2002/2003
U.S. MFN Tariff	314	35%	24%
Estimated direct payments	910	101%	70%
Equivalent tariff required if protection based only on tariffs	1224	136%	94%

Source: WTO notification and various World Bank Reports and Statistics

Table 3 **Estimated ad valorem tariff equivalent of payments received by US rice producers**			
U.S. Rice (25% broken)		*Level of Protection in ad valorem* terms	
	US$ / tonne	Assuming a world price of 175 US$/tonne 2002	Assuming a world price of 225 US$/tonne 2004
U.S. MFN Tariff	21	12%	9%
Estimated direct payments	203	116%	90%
Equivalent tariff required if protection based only on tariffs	224	128%	99%

Source: WTO notification and various World Bank Reports and Statistics

In ad valorem terms, direct payments afford an additional level of protection for US cotton and US rice that are, respectively, four and ten times above their current tariff levels. These examples clearly demonstrate the inequities that would result by the establishment of trade reforms for market access based on a simple comparison of tariffs between countries.

Moreover, the example of the EU CAP reform in the dairy sector is useful to better understand the concept of interlinkages. The effects the new positioning of the EC and the effects of price support reduction on the three pillars of the negotiations are summarized as follows:

1- **By lowering price support**, the EC will lower its trade distorting support, placing itself in a position to accept a reduction of the Aggregate Measurement of Support

(AMS). The price support[3] reduction will be compensated through a direct payment, thus meeting Blue box or Green box criteria.

2- **By lowering the support price**, the EC internal price will go down. The difference between the internal price and the world price therefore diminishes, and less support is required to finance European products outside the EC market thus less export subsidies are required.

3- **By lowering price support**, the EC internal price will go down. This has the effect of lowering the level of tariffs required to protect the internal EC market, and explains why the EC is prepared to consider a minimum reduction of tariffs.

All programs were not created equal and there is much diversity in agricultural programs across WTO member countries. Agricultural programs designs are a result of the various countries' resources, infrastructure, capital, government, market integration, and value system. Some programs may be designed in such a way that they may be more dependent on one pillar (such as the Canadian supply managed industries) than other programs that may be more balanced across the three pillars (such as the United States). This does not mean that a program is superior to another or more disruptive to trade, but simply that it is different in design. The implications of these inter-linkages are that some countries have more flexibility than others to adapt to the demands being imposed by the Framework. These inter-relationships must be properly identified, understood and defined. It is only by properly identifying the problem that appropriate solutions can be developed so that appropriate, balanced, and equitable trade reforms can be achieved in agriculture.

[3] Price support for AMS is calculated as the difference between the applied administered price (or support price) and a fixed external reference price (reflecting the world price) multiplied by the volume of production

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Discussion Paper[1]
May 2005

Market Access Package

The question of market access is highly complex and must be approached as a package. The pursuit of "substantial improvement in market access" must provide sufficient flexibility for sensitive products. As substantial improvement in market access can be achieved through various means, the market access package must be flexible enough to allow different combinations that deliver an end result that is both fair and equitable for all countries.

The following items are requirements of a "market access package":

1- A tiered reduction formula for non-sensitive products:

"Progressive income tax" formula

As stated in the Framework Agreement, a tiered approach based on the principle that the greater the tariff the greater the reduction is to be developed. A graduated tier approach based on a "progressive tax formula" would ensure a smooth transition from one tier to another and address the problem arising from tariff being at the end or the beginning of each tier. The example in the table below illustrates this point.

Tier	Rate of reduction
tariff <= 5%	5%
tariff >5%, but <= 10%	Portion <=5% - reduce by 5% Portion >5% but <= 10% - reduce by 10%
tariff >10%, but <= 15%	Portion <=5% - reduce by 5% Portion >5% but <= 10% - reduce by 10% Portion >10% but <= 15% - reduce by 15%
tariff >15%	Portion <=5% - reduce by 5% Portion >5% but <= 10% - reduce by 10% Portion >10% but <= 15% - reduce by 15% Portion >15% – reduce by 20%

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The example compares two current tariffs, 15% and 16%. Under a standard tiered formula, the 15% tariff would be cut by 15% to 13.75%, while the 16% tariff would be cut by 20% to 12.8%. As a tariff that is only 1% higher than another gets cut much more, there will be huge difficulty in establishing the tiers. In the progressive income tax formula example above the 15% tariff would get cut to 13.5%, while the 16% tariff would get cut to 14.3%. This formula generates a more equitable result

Conversion of specific tariffs into *ad valorem* equivalent
The conversion of specific tariffs into *ad valorem* equivalents is required to assess which tier a specific tariff will fall into. The purpose of the AVE exercise must only be to determine the rate of reduction that would apply to non-sensitive products.

The AVE conversion exercise should not prevent in any way a country from maintaining a specific tariff, or a combination of specific and *ad valorem* tariffs.

The decision to use the WTO IDB, in most cases provides an appropriate import unit value when trade actually occurs. The use of the IDB captures trade at the 8 digit HS level, the type of the product imported and the preference of consumers in their countries for certain products.

In those cases where the IDB data cannot be used, there are a number of other credible price sources that can be used, such as world prices, prices in neighbouring countries, export prices that can be used for specific AVE conversions.

2- A flexible approach for sensitive products that accounts for their sensitive nature.

This aspect of the market access package is crucial. It must be recognized that this provision allowed the WTO members to move forward in July 2004 and agree on the Framework for the establishment of modalities in agriculture. The following elements must therefore be considered in the selection and treatment of sensitive products.

Selection/Deviation
The selection of sensitive products must be established based on self-declaration. To ensure equity, an appropriate number of sensitive products (measured by a % of tariff lines) must be agreed upon. This "appropriate" number would serve to define the concept of deviation.

Treatment of sensitive products
Flexibility is the number one requirement in the treatment of sensitive products. Flexibility will permit better overall ambition in market access improvement. This flexibility should allow for different combinations of tariff cuts and TRQ expansion, reflecting: i) the existing commitments for these products; and, ii) the sensitivity of the product concerned.

a. Market access: as provided by the Framework Agreement, the market access provisions for sensitive products must include the possibility to select amongst combinations of tariff reductions and tariff quota commitments. For example, "0" tariff reduction for over-quota tariffs should be allowed provided that in-quota tariffs are reduced to "0" and/or provided that real market access improvements are provided; any combination should be considered, provided that market access is truly improved.

b. TRQ expansion: to address the inequities that occurred in the Uruguay Round and to ensure equity is achieved amongst sensitive products, a common minimum end point equal to 5% of domestic consumption, in a recent base period, must be agreed to.
c. Deviation: additional minimum access shall be provided according to a formula in the event a country self-selects more than the negotiated number of sensitive products.

3- Inter-linkages

Given that market access is not determined solely by tariffs, WTO negotiators must take into consideration the impact of direct payments (whether amber, blue or green). Direct payments reduce the price of locally produced goods, rendering locally produced goods more competitive and resulting in a situation where lower tariffs are required to protect domestic production. However, unlike tariffs, this trade distorting domestic support also has a negative impact on third markets. In agreeing to a tariff reduction formula, WTO members must take into account that some members have higher tariffs simply to offset the fact that they do not benefit from direct payments.

4- Special Safeguard Measures Restricted to Sensitive Products

To remain consistent with the special safeguard provisions negotiated during the Uruguay Round, and recognise the sensitive nature of the products selected as sensitive, the right to use special safeguard must be limited to and restricted to those products that have been selected as sensitive.

Products which are not selected as sensitive products (products subject to the general tariff reduction formula), should not have access to the special safeguard provisions.

5- TRQ Administration

TRQs are legitimate WTO policy tools designed to address a specific area of trade: access into markets for sensitive products. A proper functioning TRQ system depends on a common level of minimum access being offered and predictability of imports to both importing and exporting nations. Appropriate measures must be implemented to ensure the agreed level of access is achievable.

TRQs provide real market access opportunities and countries are free and should continue to be free to choose how they administer their tariff quotas. However, persistent low fill rates undermine the intent and benefit of the TRQ system. As persistently low fill rates may be due to the administration methods used, mechanisms outlining rules and disciplines related to TRQs need to be developed that would give countries the incentive to improve the administration of their TRQs. WTO members should be allowed to challenge the TRQ administration methods of an importing country, under the WTO dispute settlement provisions, and to take retaliatory measures, if they prove that those administration methods were the cause of the persistently low TRQ fill rates. Persistent underutilization of TRQs could be defined as fill rates below 75% for at least three consecutive years. However, in assessing whether fill rates are persistently low, considerations must be given to market conditions that result in lower fill rates.

As agreed to in the Framework on agriculture, all TRQ expansion in this round should be implemented on an MFN-basis. Further consideration should also be given to the elimination of country specific allocations, providing special consideration for developing countries.

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Discussion Paper[1]
May 2005

Special Agricultural Safeguard (SSG)

To remain consistent with the special safeguard provisions negotiated during the Uruguay Round, and recognising the sensitive nature of the products selected as sensitive, the right to use special the safeguard must be limited to and restricted to those products that have been selected as sensitive.

Products which are not selected as sensitive products (products subject to the general tariff reduction formula), should not have access to the special safeguard provisions.

Background

The Framework for Establishing Modalities in Agriculture states that the question of the special agricultural safeguard (SSG) remains under negotiation (paragraph 38).

Under Article 5 of the AoA, there are two contingencies for which the SSG may be invoked: a surge in the volume of imports or a sharp fall in import prices. Corresponding quantity and price triggers are defined as well as the maximum amount of additional duties that may be applied. It is also important to note:

- The SSG can only be used on products that were tariffied under the AoA *(i.e. products that would likely be qualified as sensitive products in today's terms)* and where governments reserved the right to use it in its schedule of commitments.
- SSG cannot be used on in-quota imports.

The Need for the Continuation of a SSG

Agricultural markets are cyclical and subject to wide fluctuations[2] due to weather variability, subsidization of agricultural production and exports by governments, anti-competitive behaviour of multinational corporations and external shocks caused by: exchange rate manipulations, the use of non-tariff

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[2] A Special Agricultural Safeguard: buttressing the market access reforms of developing countries. Prepared by the FAO, March 21, 2001.

barriers and the misuse of countervail & anti-dumping measures that divert normal trade flows. Such vulnerability to external shocks is of particular concern to governments, whose main responsibility is to provide for market stability: i) for farmers & downstream industries that have made substantial investments in production facilities & equipment; and, ii) to domestic & international lending institutions that have billions of dollars in outstanding loans to agricultural enterprises.

In fact, even countries that are strong proponents of "freer trade" have implemented safeguard provisions in bi-lateral free trade agreements. For example, under the United States – Australia Free Trade Agreement, the parties have agreed to a volume and price-based safeguard for beef, as well as price-based safeguard for horticulture.

Restricting the use of SSG to Sensitive Products

Access to the SSG for sensitive products must be retained, recognizing that:

1. the provisions of Article 5 of the AoA are to remain in force for the duration of the "reform process";
2. "reform" is an on-going process;
3. the risk of import surges due to the factors listed above; and,
4. the sensitive nature of products selected as sensitive.

The advantage of this approach is that it provides an important safety net for countries (with respect to their sensitive products) knowing that they can guard against sudden or unpredictable surges in imports or sharp reductions in import prices.

If countries are to be expected to accept new market access commitments on their most sensitive products there must be some mechanism for dealing with import surges or very low commodity prices that could destabilize a domestic sector, especially if that country does not have the fiscal resources to help producers.

Conversely, products which are not selected as sensitive (i.e. products subject to the general tariff reduction formula) by definition do not need access to the SSG, as those products are identified as non-sensitive. Extending or preserving the right to use SSG to non-sensitive products could, under certain conditions, create incentives to choose the general tariff reduction formula knowing that added protection is available.

Therefore, only those products that are identified as sensitive should be able to avail themselves of the SSG.

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Tariff Rate Quota (TRQ) Administration

Tariff quotas are legitimate policy tools at the WTO. They are designed to provide transparent and predictable access opportunities into selected markets. While recognizing that members do not have an obligation to import, they do have an obligation to provide unimpeded opportunity to access these selected markets.

History has shown, however, that certain administration methods of TRQ are used to restrict the level of access negotiated in the Uruguay Round. The Dispute Settlement Mechanism must therefore be strengthened to create an incentive for members to address the inefficiencies in some tariff quota administrative procedures.

In the case of persistently low fill rates, countries should be allowed to formally challenge the TRQ administration methods of an importing country.

Background

Under paragraph 35 of the WTO Framework for establishing modalities in agriculture, the question of operationally effective improvements in TRQ administration is identified as one of the key elements that will give flexibility to enable members, and particularly developing country members, to fully benefit from the market access opportunities under tariff rate quotas. Chairman Groser stated that the Harbinson text will serve as the basis for discussing and negotiating possible disciplines leading to improvements in tariff quota administration.

Tariff quotas are legitimate policy tools at the WTO that are designed to provide transparent and predictable access opportunities into selected markets. While recognizing that members do not have an obligation to import, they do have an obligation to provide unimpeded opportunity to access these selected markets.

The Harbinson text provides guidelines that attempt to tighten the rules for administrating TRQs and to clarify members' obligation to ensure that market access opportunities are made fully and effectively available in a fair and equitable manner. However some provisions contained in the Harbinson text go

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beyond this objective and encroach on members' rights to select the administration method best suited to their domestic agricultural policy. In order to ensure an efficient TRQ administration, countries can not be dictated a select list of approved methodologies that would not correspond to their situation. The emphasis must be on the fill rates as the way to measure effective access.

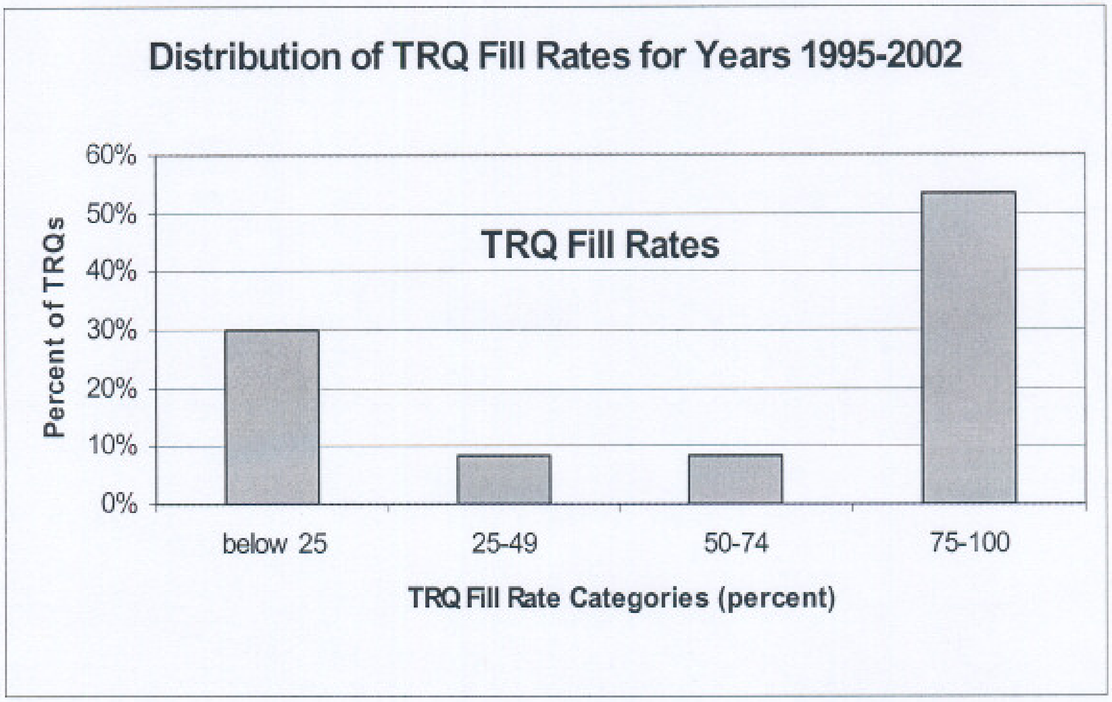

Figure 3: The distribution of all reported average fill rates reveals a bimodal pattern with the majority of the notified fill rates falling into the lowest (fill rates of less than 25%) or highest (fill rates of 75% or greater) range categories. Fill rates were calculated for all commodities in all product groups from 1995 – 2002, based on the notifications to the WTO as of January 2004. Total number of observations: 7210.

Specific Requirements for Establishing Improved Tariff Quota Administration Procedures

There are several methods by which tariff rate quotas (TRQs) are administered. No particular method is presumed to be acceptable in all circumstances. The following disciplines must govern tariff rate quota administration procedures by WTO members:

1. WTO members must notify on a timely basis the annual volume of imports, TRQ fill rates and the administration method[2] used for allocating each TRQ as specified in their schedule of commitments, as well as up-to-date information on the current status of fill.

[2] Examples of various administration methods used include: First-come/First-served; Licenses on Demand; Auctioning; lottery.

2. All and any formalities and requirements[3] governing TRQ administration must be publicly available in a timely manner, by means of a website or through a single window government access point, to domestic importers and other WTO members.

3. Formalities and requirements must not be used in a manner that would prevent minimum access commitments under the TRQ from being fully achievable.

4. In order to ensure that WTO members' minimum access commitments are available to all WTO members, TRQ specific allocations must be eliminated without creating member countries' obligations in excess of their WTO commitments.

5. Taking into consideration the variety of TRQ administration methods used and the right of WTO members to establish domestic agricultural policy, members must retain the right to administer TRQs in accordance with the following basic conditions provided that the administration method formalities and requirements governing TRQ administration chosen do not restrict the overall level of minimum access agreed upon:
   a) To designate the domestic market segment(s) that receive import quotas;
   b) Use of State Trading Enterprises (STE's) and other agents to administer TRQs;
   c) Use of past trading performance, domestic purchases and other trading criteria as an eligibility requirement for securing shares of TRQ allocations where allocated to domestic importers;
   d) Limits on TRQ shares where allocated to specific importers.

6. Where TRQs are allocated to domestic importers, WTO members must implement and notify the measures implemented to ensure full utilization of the TRQ.

7. Where annual TRQ fill rates are continuously and significantly less than the TRQ as specified in a member's schedule of commitments, full opportunities for consultations must be provided.

Required Amendments to the Harbinson text

The selection of TRQ administration method must remain at the discretion of the importing member, as long as the implemented methods and practices are consistent with existing rules and do not impede agreed access. These realities must be reflected in the provisions suggested by Harbinson.

Dispute Settlement Mechanism

Persistently low fill rates undermine the intent of the TRQ system and can be an indication that a country needs to improve the management of its system. While market conditions may preclude imports into a selected market, it must be recognized that fill rates may be persistently low due to the administration method implemented.

[3] TRQ Formalities and requirements include such aspects as the size of the quota allocation and the period of licence validity.

The dispute settlement provision must be strengthened to create an incentive for members to address the inefficiencies in their tariff quota administrative procedures. In particular, countries should be allowed to formally challenge the TRQ administration methods of an importing country. In the case of persistently low fill rates, the dispute settlement mechanism should apply.

Persistent underutilization of TRQs could be defined as fill rates below 75% of the TRQ for at least three consecutive years.

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Discussion Paper[1]
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Selection and Treatment of Sensitive Products

The treatment of sensitive products must be completely separated from the general tariff reduction formula. Linking the treatment of sensitive products to the general tariff formula would negate the recognition of sensitive products and would result in a situation where sensitive products are treated more severely than non-sensitive products.

The Framework Agreement states that "substantial improvement will be achieved through combinations of quota commitments and tariff reductions applying to each product", and that "balance in this negotiations will be found only if the final negotiated result also reflects the sensitivity of the product concerned." Flexibility is therefore required.

The Framework Agreement also calls for tariff quota expansion for all sensitive products taking account of coherent and equitable criteria. These criteria must allow sufficient flexibility to address the sensitivity of these products while addressing the inequities that resulted in the Uruguay Round: specifically, a common minimum level of access must be offered for sensitive products.

In the pursuit of equity, consideration must be given to the concept of "deviation" which must be measured relative to an agreed upon "reference number" of sensitive products. Countries would be permitted to select a greater number of such products by offering a higher level of access as compensation.

The recognition that WTO member countries have sensitive products was crucial in obtaining the necessary consensus to achieve the July 2004 Framework Agreement.

The fact that sensitive products are addressed under their own heading within the market access pillar:

- underscores the fact that these products are sensitive; and,
- more importantly, reinforces the fact that they must be treated separately from other (i.e. non-sensitive) products.

[1] This is a discussion document; it is not a statement of approved policy by the author organizations of affiliates.

Selection

- The selection of sensitive products must be established on a self-declaration basis

Treatment of Sensitive Products

Combinations of tariff reduction and TRQ expansion

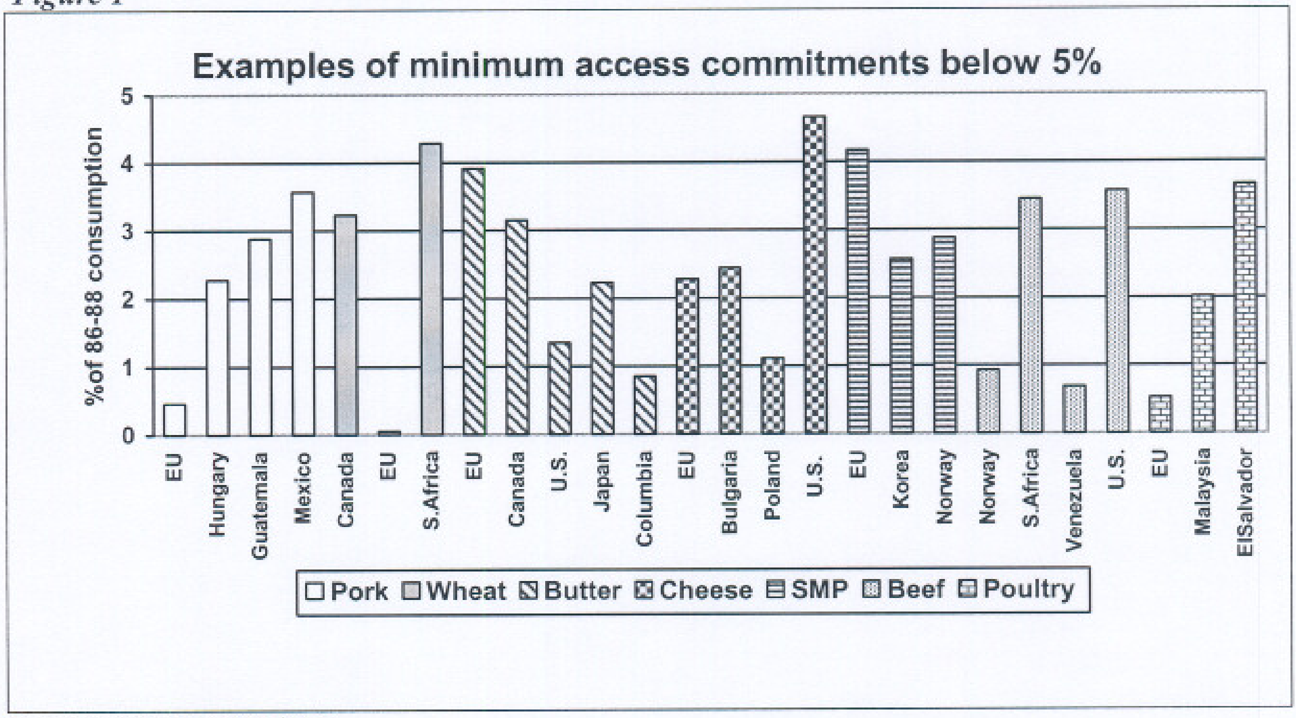
As provided by the Framework Agreement, the market access provisions for sensitive products must include the possibility of trade offs, through combinations of tariff reductions and tariff quota commitments. For example, "0" tariff reduction for over-quota tariffs should be allowed provided that in-quota tariffs are reduced to "0" and/or provided that real market access improvements are provided; any combination should be considered, provided that market access is improved.

TRQ Expansion

Figure 1 provides a number of examples of minimum access commitments. The average access for all WTO tariff rate quotas (TRQs) is about 3.3% of domestic consumption. In addition, when considering fill rates, the effective level of access is closer to 2%.

Proper attention must be given to how the criteria for tariff quota expansion will be developed. In order for the criteria to be considered coherent and equitable it must result in an equitable and achievable minimum level of market access commitments, equal to 5% of domestic consumption, in a recent base period. The reference to 5% of domestic consumption is a realistic goal given that, despite agreement in the Uruguay Round, most countries fall below this mark (see figure 1).

Figure 1



Source: AMAD Database

In the August 1, 2004 Framework Agreement, WTO members agreed that for sensitive products "some MFN-based tariff quota expansion will be required". They also agreed that the base for this expansion will be established taking account of "coherent and equitable criteria".

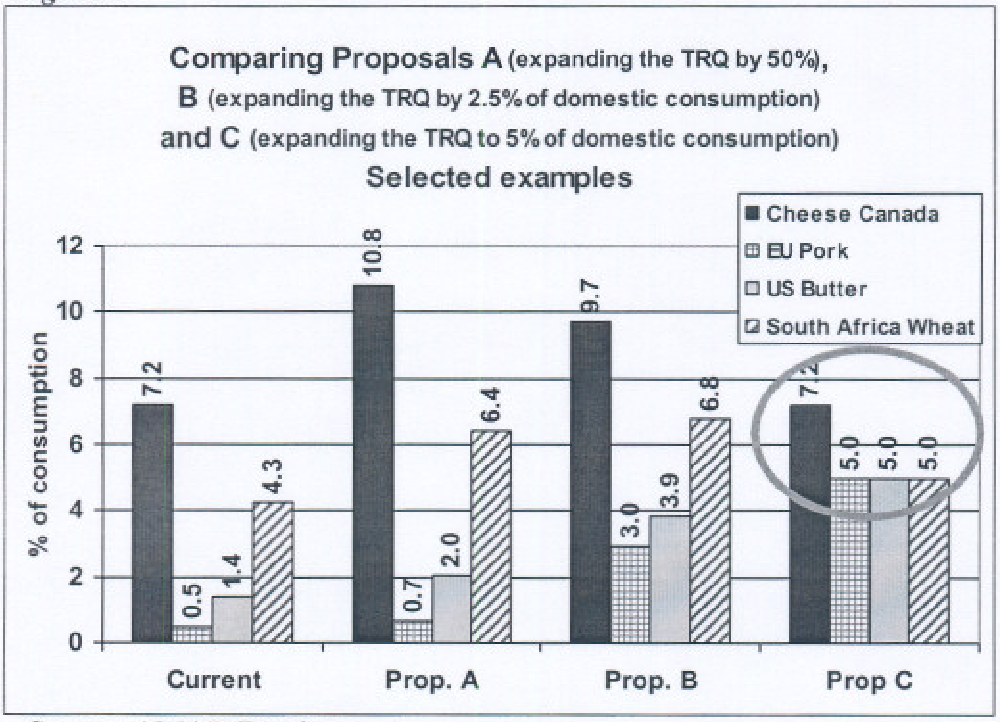
Since the launch of the Doha Round, there have been a myriad of proposals tabled by WTO members aimed at "substantial improvements in market access". However, these proposals can be summarized as follows:

Proposal A)	Expanding existing TRQs **by** (x)%
Proposal B)	Expanding existing TRQs **by** (x)% of domestic consumption in a given period
Proposal C)	Expanding existing TRQs **to** (x)% of domestic consumption in a recent base period (Re-basing)

Figure 2 provides a comparison of the three proposals. To facilitate the comparison, we have made the following assumptions:

Proposal A)	Expanding existing TRQs by 50%;
Proposal B)	Expanding existing TRQs by 2.5% of domestic consumption – a 2.5% expansion should technically be equivalent to a 50% increase under proposal A); and
Proposal C)	Expanding existing TRQs to 5% of domestic consumption in a recent base period

Figure 2



The rebasing option reduces current iniquities.

Source: AMAD Database

Proposal C has the advantage of ensuring all countries are treated fairly, larger increases in access for those countries/commodities where current access is the least - it provides for greater equity.

Given that the data used by WTO members to establish access commitments is almost 20 years old, commitments from the Doha Round should be updated to reflect the most recent data available (re-basing).

Subjecting the criteria for tariff quota expansion to a rules-based common minimum end point of the domestic consumption in the most recent years for which data is available meets the objective set in the Doha mandate which calls for "substantial improvements in market access". It also meets the parameters set in the Framework Agreement calling for the development of coherent and equitable criteria.

Deviation

Paragraph 31 of the Framework states that members may designate an appropriate number of tariff lines to be treated as sensitive. Paragraph 34 states that "MFN based tariff quota expansion will be provided under specific rules to be negotiated taking into account deviations from the tariff formula". Linking the concept of deviation to the number of sensitive products (measured in terms of tariff lines) would be a step in ensuring that sensitive products are treated differently and appropriately.

While the selection of sensitive products should be on a self-declaration basis, an appropriate reference number will have to be negotiated. Allowing a large percentage of tariff lines to be treated as sensitive would thwart the willingness to provide adequate flexibility in the treatment of sensitive products. Conversely, if those countries with a very high number of sensitive products were not allowed to declare them as sensitive, they would be less likely to agree to an ambitious general tariff reduction formula for non-sensitive products.

As a result, negotiating an "appropriate" number of sensitive products is essential. Therefore, WTO members will have to agree to a reference number of sensitive products for which a common level of market access (based on domestic consumption) has to be provided. Those with higher numbers of sensitive products would have to provide additional access for those products. In other words, additional access would have to be proportional to the number of sensitive tariff lines in excess of the reference number.

The following table shows how this could work:

Number of sensitive Products	*Minimum level of access*
Equal to or Less than the Reference number: x%	*x% of domestic consumption, per product*
Additional z%	*Additional x% of domestic consumption, per product*

For example, for countries with a number of sensitive products equal to or less than the reference number, the level of access would be x% of domestic consumption.

With respect to deviation, for each additional percentage of tariff lines above the reference number (shown as *z%* in the table), countries would have to provide additional access equal to x% of domestic consumption.

The treatment of sensitive products must be completely separated from the general tariff reduction formula, reflect the sensitivity of the product concerned, and be treated more favourably than other products.

Canadian dairy, poultry & eggs

Secteurs canadiens des produits laitiers, de la volaille et des œufs

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1101-75 rue Albert St.
Ottawa ON K1P 5E7
T • (613) 236-9997
F • (613) 236-0905

Chicken Farmers of Canada / Les Producteurs de poulet du Canada
1007-350 rue Sparks St.
Delta Office Tower
Ottawa ON K1R 7S8
T • (613) 241-2800
F • (613) 241-5999

Canadian Egg Marketing Agency / Office canadien de commercialisation des œufs
1501-112 rue Kent St.
Ottawa ON K1P 5P2
T • (613) 238-2514
F • (613) 238-1967

Canadian Turkey Marketing Agency / Office canadien de commercialisation du dindon
7145 avenue West Credit Avenue
Bldg./Bâtiment 1, Suite 202
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T • (905) 812-3140
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Canadian Broiler Hatching Egg Marketing Agency / Office canadien de commercialisation des œufs d'incubation de poulet à chair
1101-75 rue Albert St.
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Discussion Paper[1]
May 2005

Domestic Support

The 2004 Framework Agreement calls for substantial reductions for supports that distort trade, and places limitations on the three categories of trade distorting support: amber, blue and *de minimis*. As a result of the artificial categorization of trade supports, countries have focused their efforts not on reductions of domestic supports, but on developing trade supports that could be classified under blue box and green box measures. An approach that (1) addresses the trade distorting impacts of domestic support, (2) reduces the potential for box shifting, and (3) uses value of production as a measure to determine commitments is the best means of achieving balance and equity between trading partners.

Introduction

The introduction of disciplines on the use of domestic subsidies is an important element of the trade reforms being pursued. Some forms of domestic support are considered to be problematic because it is thought to subsidize production by creating a higher internal market price which then, in the absence of production controls, may lead to overproduction and the need to dump on the world market. Unfortunately, the importance of domestic support as an important rural development tool both for developing countries and developed countries has been minimized.

The artificial categorization of trade supports has shifted the focus from reducing the impact of domestic supports on world markets to developing trade supports that could be classified as blue box and green box measures. The framework attempts to limit the amount of domestic support box shifting that will be possible by mandating that caps be placed on amber product specific support, on blue box support, and that the permitted *de minimis* support be reduced. Approaches on how to institute these reforms in a manner that results in greater equity between members are presented here and include:

1. A Two Filter Approach for Amber Product Specific Caps;
2. A Historical Cap: An Inequitable Measure;
3. The Creation of a Common Cap for Blue Box and *De Minimis*; and
4. Green Measures Inclusion in Overall Reduction in Domestic Support

[1] This is a discussion document; it is not a statement of approved policy by the author organizations of affiliates.

1. A Two Filter Approach for Amber Product Specific Caps

A product specific cap, as is proposed by the 2004 Framework Agreement, is not an ideal solution for domestic support reforms. The interconnectedness of the world marketplace makes agricultural commodity sectors more vulnerable to risk, and a product specific cap reduces the flexibility countries currently have to respond to agricultural sectors in times of crises.

However, if a product-specific cap is applied, an approach that links the obligation to reduce support to the trade distorting impact of that product on world markets would result in the greatest equity. Such an approach would address the negative impact that some support has on world markets while not undermining the choice of developed and developing countries to use domestic support as a tool for rural development.

The proposed approach consists of two filters. The first identifies which products have the highest levels of domestic support as a percentage of the product's value of production, and the second tests the trade distorting threshold of that product. The product must be caught by ***both*** filters to be subject to support reductions.

Filter One: Support as a % of Value of Production

If a country's amber product specific support is:

≤X% of value of production,	no capped is imposed.
> X% of the value of production,	go to a second filter.

Filter Two: Exports as a % of World Exports

If a country's total exports of the product are:

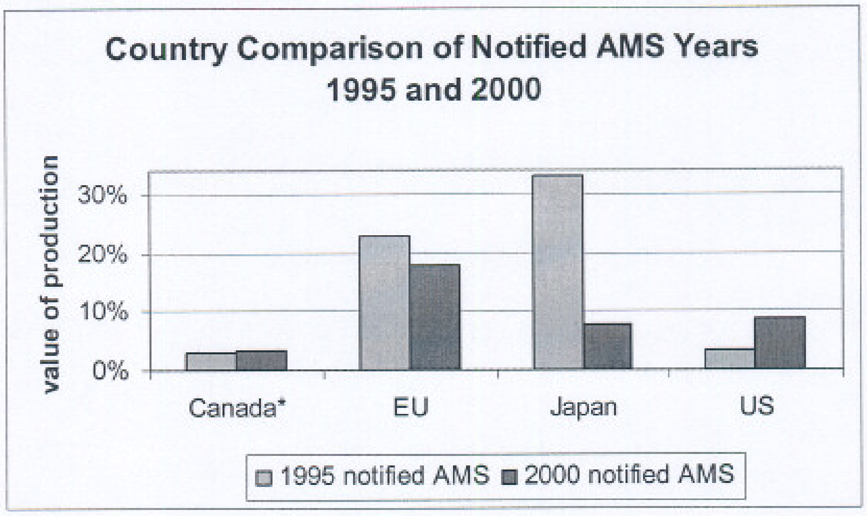
≤Y% of total world exports of that product	no cap is imposed.
> Y% of total world exports of that product,	countries must reduce product specific support to X% of value of production.

This would allow flexibilities to countries like Norway that have relatively high levels of domestic support, but that have low levels of exports and therefore little impact on depressing world prices. In cases where there is trade distortion, as measured by the filters, moving to common end-points would promote greater equity between participants in the world markets as all countries would be playing on a level playing field.

2. A Historical Cap: An Inequitable Measure

Reductions based on historical levels are unacceptable if the Doha Round's goal of increased equity between members is to be achievable. Any kind of cap, whether it is on overall support or category support, must be applied on a value of production basis and not on historical averages. If not, inequities, such as those resulting from the Uruguay Round will be repeated.

A cap on a value of production basis would be more equitable as it would reward countries that have kept their level of subsidization at a minimum compared to those that currently subsidize a significant portion of their agriculture. By examining trends in notified domestic support on a value of production basis, it is made clear that while most countries have made efforts to reduce domestic support and have succeeded or remained close to the same level of support on a value of production basis, others have increased their spending. For example, Japan has made large reductions in domestic support, while the United States has increased the amber support to its farmers since 1995. This is depicted in figure 2.



*2000 notification for Canada unavailable, therefore 1999 notification used

Figure 2: Notifications of amber support, expressed as value of production, show that some countries have made efforts to reduce amber support, while others have not.

The picture is similar on a product specific basis. A comparison between countries reveals the huge inequities that could result from the establishment of a cap based on historical averages.

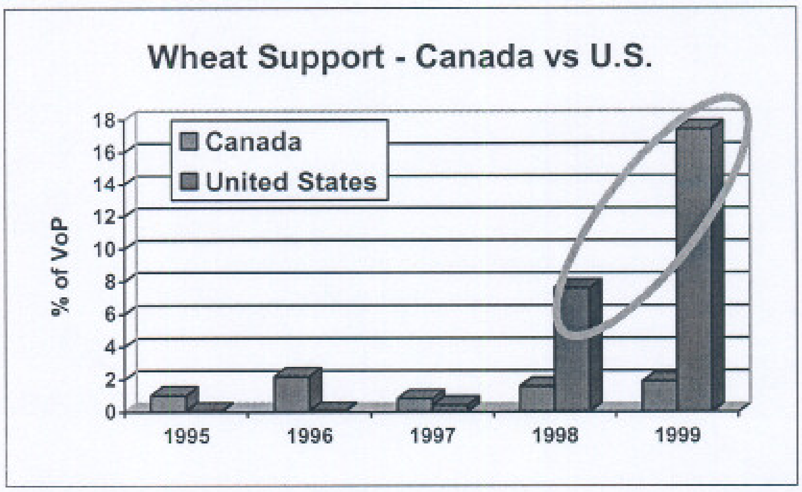


Figure 3: A cap based on historical averages would confer a huge advantage to the United States over Canada on the flexibility to provide support in wheat.

Lastly, a product specific cap based on historical levels reduces flexibilities. An example of this can be drawn from the experience of the beef cattle industry. From 1995 through 2000, the level of support in the beef industry in Canada fluctuated between 1 and 2% of the value of production. Had that support been capped at historical levels, Canada would not have been in a position to deal with the BSE crisis it has been experiencing in the past few years.

3. The Creation of a Common Cap for Blue Box and *De Minimis*

A single cap of 5% of the value of production, to cover both the new blue box and *de minimis* would have a more equitable and effective impact on reducing the potential for box shifting than the approach proposed in the 2004 Framework Agreement. The Framework's mandate to apply product specific caps on amber support measures based on a historical basis threatens to create inequities between members in several ways. Box shifting is a flexibility that some countries will have and some will not. Countries with large treasuries, such as the U.S. and the E.U, when faced with the obligation to cut their AMS, are in positions to redesign programs that will allow them to shift support from the amber box to the blue box in order to circumvent their AMS reduction obligations. Disparities between members will increase as big spenders are in a position to take advantage of the loophole that box shifting will provide. The example depicted in Table 1 uses information notified by the U.S. for domestic support to demonstrate the flexibility the U.S. could have if it maximized its *de minimis* and blue box allowance.

Table 1: US Example of Flexibility Available Through Box Shifting

Current situation (based on the US 2001 WTO Notification):	
• Value of agricultural production	198.5 billion USD
• Current AMS	14.4 billion USD
• *De minimis* (5%; product specific and non-pr. sp)	6.8 billion USD
• Blue Box (unlimited)	0.0 billion USD
• **Total trade distorting**	**21.2 billion USD**
• Total AMS Commitment	19.1 billion USD
Potential Post-Framework situation:	
• Value of agricultural production	198.5 billion USD
• *De minimis* product specific[2] (max 2.5%)	5.0 billion USD
• *De minimis* non-product specific[3] (max 2.5%)	5.0 billion USD
• Blue Box (max 5%)	9.9 billion USD
• Total AMS Commitment (93% cut)	1.3 billion USD
• **Allowable trade distorting**	**21.2 billion USD**

It is assumed that a new blue box capped at 5% of the value of production and a new *de minimis* level of 2.5%[4] of the value of production would allow the U.S. to spend 19.9 billion USD. This represents 94% of the current U.S. trade distorting spending. The remaining 6% of distorting

[2] For illustration purposes only. Canada does not support the reduction of *de minimis* support
[3] For illustration purposes only. Canada does not support the reduction of *de minimis* support
[4] For illustration purposes only. Canada does not support the reduction of *de minimis* support

support (1.3 billion USD) represent only 7% of the U.S. Total AMS commitment. This means that the U.S., while respecting all the provisions of a new agriculture agreement, can undertake a 93% cut in its AMS commitment without impacting on its actual domestic support spending!

This process is counter to the objectives set for the Doha Round and simply gives additional advantages to those who are the largest spenders and whom have the largest treasuries. The changes to *de minimis* and the cap on blue box proposed by the July Framework will likely have little effect on those these reforms are meant to target. Within a single cap of 5%, WTO members should have the flexibility to choose what types of measures they wish to use, whether blue or *de minimis*, in order to respond to the particular needs of their domestic sectors.

4. Green Measures Inclusion in Overall Reduction of Domestic Support

The 2004 Framework Agreement also tries to limit the potential for box shifting by calling for an overall reduction in trade distorting domestic support which it defines as the sum of amber, blue, and *de minimis* supports. While this is a step in the right direction, it can be argued that these global reductions in support must include green measures if box shifting is to be limited and greater equity between members is to be achieved.

All forms of support, including green, confer an advantage, either indirectly or directly, to a producer. With the onset of a "color" debate on how *"blue is blue"* and how *"green is blue"*, the likelihood of support simply being shifted from one box to another is high. For example, the United States is quickly redesigning many of its amber programs to fit blue box criteria and will likely exert a great deal of pressure to ensure that any revised definition of blue box measures will fit its program designs. A recent publication from the Estey Centre Journal of International and Trade Policy reported that the EU believes that the new Single Payment Scheme, which replaces the former system of area and headage payment to farmers, tied to production, will qualify for green-box status in the WTO.

A possible solution is to apply an approach that:

1. reduces the gains achieved through box shifting by creating a new category of domestic support that would include amber, blue, *de minimis*, and green measures; and,
2. requires reductions to a common minimum endpoint when total domestic support levels (measured as a % of value of production), in combination with export levels, are found to be trade distorting (perhaps similar to the two-filter approach described in section one)

Conclusion

The concepts that have been put forth here attempt to approach domestic support reforms in a relevant, equitable, and straightforward manner. At the same time, these concepts attempt to preserve the autonomy for countries to organize themselves domestically as they wish, provided it does not distort world markets.