RESTRICTED

MULTILATERAL TRADE NEGOTIATIONS THE URUGUAY ROUND

MTN.GNG/NG5/W/97
10 July 1989

Special Distribution

Original: English

Group of Negotiations on Goods (GATT)
Negotiating Group on Agriculture

DISCUSSION PAPER ON TARIFFICATION SUBMITTED BY THE UNITED STATES

I. Introduction

According to the recent Mid-Term Agreement, the objective of these agriculture negotiations is to establish a "fair and market oriented agricultural trading system" and "provide for substantial progressive reductions in agriculture support and protection... resulting in correcting and preventing restrictions and distortions in world agricultural markets." This objective is to be achieved through the negotiation of strengthened and more operationally effective GATT rules and disciplines and commitments on support and protection encompassing "all measures affecting directly or indirectly import access and export competition" - i.e. import barriers, internal support measures, export subsidies, and export prohibitions and restrictions. The purpose of this paper is to show how tariffication - the conversion of non-tariff import barriers to tariffs - can be used as a means to accomplish these goals.

The United States is pleased that contracting parties have agreed to include all aspects of agricultural support and protection within the scope of these negotiations. As we have indicated in our earlier submissions, we believe that effective reform of the agricultural trading system will require such a comprehensive approach. This paper will focus on import barriers only. Over the coming months, other United States submissions will cover internal support, export subsidies, and export restrictions. contracting parties should view tariffication and the subsequent reduction of tariffs as part of a comprehensive package that must include fundamental reforms in all other policy areas. Because domestic policies can substitute for and work in conjunction with import barriers, it is necessary that any reduction in protection be accompanied by parallel reforms in internal support and export subsidies.

II. Rôle of tariffication

With respect to import access, the Mid-Term Agreement states that measures addressed should include "quantitative and other non-tariff access restrictions, whether maintained under waivers, protocols of accession or other derogations and exceptions, and all measures not explicitly provided for in the general agreement". Ministers also agreed that commitments negotiated should encompass the matter of conversion of these measures into tariffs. The United States first proposed the conversion of non-tariff import barriers (NTB) to tariffs in its submission of 9 November 1988 (MTN.GNG/NG5/W/83). We see the concept as the logical first step in the reduction in agricultural protection and an indispensable element in an effort to bring agriculture trade more fully under GATT disciplines.

Bound tariffs are the preferred method of import protection under the GATT. Existing GATT rules, however, have not been sufficient to prevent the use of NTBs in the agriculture sector. The United States, therefore, proposes that equivalent tariffs replace all existing NTBs to import access. Conversion to tariffs will enable GATT rules to be changed to remove agriculture-specific derogations with respect to NTBs and to extend disciplines to measures not explicitly provided for under the GATT. In addition, tariffication will permit the elimination of all waivers, protocols of accession or other derogations or exceptions that allow the maintenance of NTBs.

Tariffs are the least trade-distortive type of import barrier. They establish a direct link between domestic and world market prices and allow the transmission of world market signals. Most non-tariff measures are designed to stabilize internal prices by shifting to external markets the burden of adjusting to changes in supply or demand. Exclusive reliance on tariffs would ensure that the burden of adjustment is spread over all markets, thereby making world market prices more stable and predictable.

Tariffs have other advantages: unlike most quantitative restrictions, they produce revenue for governments, and they do not require licensing or other cumbersome and costly forms of government interference. Finally, tariffs are more transparent than non-tariff barriers. This transparency tends to promote trade and allows foreign suppliers to compete against one another on the basis of quality, cost, and price, free from administrative constraints and discrimination between suppliers.

While tariffication alone could have a liberalizing effect, the United States views conversion to tariffs as a means to an end rather than an end in itself. A commitment to proceed with tariffication should anticipate the substantial progressive reduction of tariffs. At an appropriate point in the negotiations, the United States will submit a follow-up proposal to the negotiating group outlining a method for tariff cutting and schedules for implementation of the cuts.

III. Methodology

If all NTBs are to be converted to tariffs, there is, of course, a need to discuss the way in which conversions will be accomplished. A standardized methodology will facilitate the process of converting NTBs to tariffs and will guide contracting parties in calculating their own tariff equivalents and in evaluating the calculations of others.

Every non-tariff import access barrier has an implicit tariff equivalent that bears a relationship to the price gap between the world price for the protected commodity and the internal price. But it will not be possible to devise a methodology for tariff conversion that would assure countries that they would be able to limit import penetration, even in the short-term, to the same level that had been provided by the non-tariff access barriers. Unlike quota or variable levy systems, import penetration under tariff increases (or decreases) as world market prices fall (or rise). It is possible, however, to construct a tariff level that will approximate the degree of import penetration offered by non-tariff measures during a given reference period.

In most cases, the following formula could be used to calculate ad valorem tariff equivalents for an NTB. (This formula yields an ad valorem tariff equivalent; however, specific duties could be used as well.)

$$TE = [(Pd-Pw)/Pw] \times 100$$

where TE is Tariff Equivalent
Pd is Domestic Price
PW is World Price

IV. Examples

A quota increases domestic prices by reducing the amount of supply available to consumers at the world price. The difference between the world price and the higher domestic price is equivalent to a tariff of that amount. If the domestic price for the product in question during the reference period is 100, and the world price is 50, the tariff equivalent would be 100 per cent = [(100-50)/50] x 100.

In the absence of an explicit quota, import licences can be used to ration the amount of import supply available to consumers at the world price. This reduction in domestic supply also raises the domestic price. The method of converting import licences into tariffs, therefore, is similar to that for converting import quotas.

The ad valorem equivalent of a variable levy (VL) is often calculated by comparing the average level of the VL over a given reference period to the average world price over the same period. In most cases, however, this methodology would yield a higher tariff equivalent than the price gap methodology. This is because VLs typically represent the difference between an administratively fixed price (threshold price) and the world price, and the threshold price is significantly higher than the domestic price.

For example, if the threshold price for a given product during the reference period is 100, the domestic price is 80 and the world price is 50, the tariff equivalent using the average VL would be 100 per cent = [(100-50)/50 x 100, but using the price gap approach it would be 60 per cent = [(80-50)/50] x 100. In order to ensure that producers benefiting from the VL are not allowed a larger margin of protection after tariffication than producers protected by quotas or other NTBs, the price gap methodology should be used for converting the VL as well.

V. Issues involved in tariffication

Despite the apparent simplicity of the price gap methodology, the United States recognizes that there are a number of technical and policy issues associated with tariffication that must be addressed. Some of the most important of these are discussed below.

A. Reference prices - In order to figure the price gap for a given commodity, two prices are needed - a domestic price and a world price. In most cases, the appropriate figures should be available. However, such data may not exist in all cases, and alternative procedures will need to be developed for such cases. The following comments are intended to identify some of the issues which may arise as countries attempt to develop appropriate price series:

1. An observed price series may not exist for all commodities. For example, price series may exist for one type or quality of cheese, but not for all types or qualities of cheese. In such cases, prices would need to be adjusted to account for major differences in quality or other technical characteristics.

2. The selection of an appropriate world price may be difficult. If some trade occurs for the commodity, a world reference price could be based on the c.i.f. import price (unit import value) derived from standard trade statistics. If no imports occurred during the base period, an approximation of the world price will need to be developed from observed prices in the international market. One approach could be to use the f.o.b. price of a major exporter of the specific commodity with appropriate transportation and handling adjustments to the border of the country in question.

3. The choice of appropriate domestic prices may also raise some issues. For example, domestic prices should represent the commodity at the same stage of processing as the traded product. If appropriate prices do not exist, the farmgate price could be adjusted to account for the processing undergone by the imported product.

B. Base period - since the magnitude of the price gap can fluctuate widely from year to year depending on changes in reference prices, the choice of base period used in the calculation of the initial tariff equivalents will be important. Using 1986, when the negotiations began, as a base period would lead to significant distortions, since world prices for most commodities have risen significantly in the past three years. Conversions made on the basis of 1986 prices would result in an immediate, significant jump in import protection in many cases and could seriously disrupt world trade. Using the most recent year that is not distorted by drought or other exceptional circumstances and for which data are available would provide a more accurate approximation of the current levels of protection.

C. Operation of domestic programmes - many of the NTBs currently in use are designed to facilitate the functioning of domestic price support programmes. High internal price supports often give rise to surpluses that are frequently exported using subsidies. In order to correct and prevent distortions in world agricultural markets, it will be crucially important to accompany reductions in tariff equivalents of NTBs with equivalent actions on internal support and export subsidies.

D. Product standards - as tariffication proceeds, some countries may be tempted to impose new import restrictions in the form of product standards such as sanitary and phytosanitary restrictions. This highlights the importance of the initiative to harmonize sanitary and phytosanitary regulations that is mandated in the Mid-Term Agreement. It may be necessary to monitor the use of other technical barriers to trade as well (e.g. quality standards, labelling requirements) to ensure that there is no abuse of such measures.

E. Policy coverage - as indicated above, tariffication is intended to apply to non-tariff import barriers only - policies such as quotas, variable levies, import restrictions or prohibitions administered in connection with marketing boards and State-trading operations, voluntary restraint agreements, restrictive licensing practices, and other import restrictions and prohibitions. It would not apply to internal support policies - such as price supports, deficiency payments, production subsidies and input subsidies - or to export subsidies. The United States recognizes that trade distortions resulting from such policies must be concurrently addressed. We intend to submit proposals dealing with these trade-distorting policies later this year.