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# Implications of the WTO on the Redesign of U.S. Farm Policy

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# Implications of the WTO on the Redesign of U.S. Farm Policy

## **Abstract**

The WTO commitments made by the United States are often cited as being an important constraint on the design of future U.S. farm programs. Many, however, are confused about the U.S. commitments and their future importance. In this paper, the authors attempt to fill this gap in understanding by providing a detailed explanation of the WTO agreement and estimates of whether the United States has fully complied with its WTO commitments in recent years. In addition, the authors project the degree of compliance through the 2002 marketing year and examine new alternative program proposals to determine how they might impact U.S. compliance.

## **Disciplines**

Agricultural and Resource Economics | Agricultural Economics | Agriculture Law | Economic Policy | International Economics | International Trade Law

# Implications of the WTO on the Redesign of U.S. Farm Policy

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# IMPLICATIONS OF THE WTO ON THE REDESIGN OF U.S. FARM POLICY

## Introduction

**C**urrent U.S. farm policy expires in September 2002. The debate over a new farm bill has begun in earnest with hearings in the Agriculture Committee of the House of Representatives. Commodity groups have begun to present their ideas and proposals for policy changes. One reason for this early start to changes in farm policy is that many people (both within and outside of agriculture) see this year as an opportunity to increase agriculture's base federal budget. The opportunity arises both because Congress has substantially increased spending on agricultural programs the last few years on an emergency basis and because the federal budget is running in surplus. Both of these trends are shown in Figure 1.

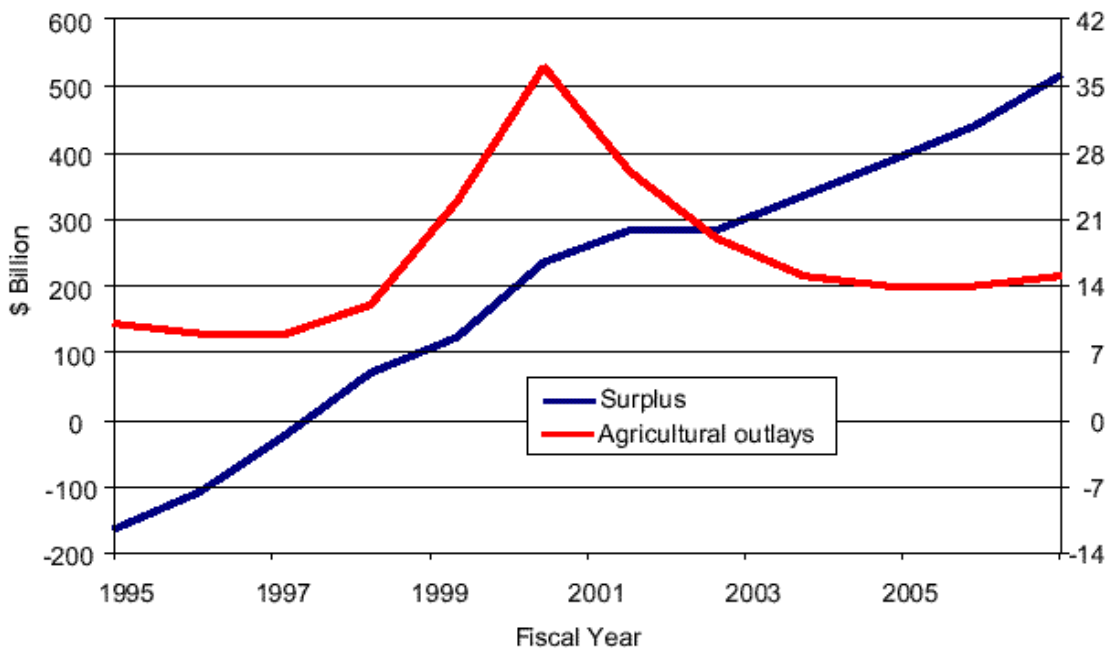
With each new farm bill, the array of federal agricultural programs is modified. New programs are added while some existing programs are changed or eliminated. Individual programs are designed to address a given issue in agriculture. The federal crop insurance program provides producers with subsidized insurance for their crop yields and/or revenues. Marketing loan programs guarantee farmers a minimum price for their products. The Production Flexibility Contract (PFC) payments provide income support to the agricultural sector.

The emergency agricultural support packages of the last three years have led many to conclude that the current farm program does not provide adequate support to farmers and

that federal agricultural expenditures are too low. Thus, many are looking to change the existing policy, which was created when the federal budget was projected to be in deficit spending. The proposed changes range from modifications of existing programs to creation of new ones.

Much of the discussion thus far has focused on the countercyclical nature (or lack thereof) of farm programs. Within the current programs, the marketing loan and crop insurance programs are countercyclical because expenditures increase in response to a decline in either price or yield. Marketing loan payments increase with lower prices. Crop insurance indemnities accrue when yield and/or revenue falls below set levels. PFC payments are not countercyclical because they are fixed throughout the life of the program.

Proposals to increase the loan rates or rebalance them (raise some to a level so that they are more acreage neutral) have been made by at least 20 farm groups and are being considered within numerous bills before Congress (for example, House Resolution 32, Senate Bill 20, and Senate Bill 165, 107th Congress). Any increase in commodity loan rates would increase program payments due to low prices. In addition, some of the proposals eliminate payment limits, thereby further increasing program payments. House Resolution 32 outlines the flexible fallow program (analyzed in CARD Working Paper 00-WP 263



Note: The budget surplus numbers are given on the left axis. The agricultural outlays are given on the right axis.

**FIGURE 1. Federal government budget surplus projections and agricultural outlays**

and FAPRI-UMC Report #13-99) where producers receive higher loan rates for idling a portion of their land.

The Commission on 21st Century Production Agriculture, in its report to Congress, proposed a revenue-based countercyclical federal farm program. The proposed program would compare current gross income from the eight major crops (barley, corn, cotton, oats, rice, sorghum, soybeans, and wheat) to a percentage of a fixed-base historical income from the same crops. Producer eligibility would be determined by historical production, and payments would be based on fixed acreage and yields. The Commission's proposal was derived from two earlier proposals, the Supplemental Income Payments (SIP) program, introduced by Rep. Stenholm (D-TX) (House Resolution 2792, 106th Congress), and the Supplemental Income Assistance

Program (SIAP), put forward by the Clinton administration. In these earlier variations, program parameters and payments would be crop specific.

Programs to base payments on farm-level environmental performance have also been proposed. The Conservation Security Act of 1999 (Senate Bill 1426, 106th Congress) would have provided payments to agricultural producers for resource conservation and livestock nutrient management plans. The size of the payments would vary according to average land rental rates or livestock prices in the region and the practices taken by the producer. These payments would be capped but would supplement any PFC payments the producer receives.

The U.S. Department of Agriculture (USDA) examined several possible safety net programs based on farm income (USDA-

ERS AER-788). In each of these programs, farm households were assured a certain level of income. Four different income targets were chosen:

1. the median nonfarm household income in the region,
2. 185 percent of the poverty level,
3. the average nonfarm household's annual expenditures, and
4. the income level from the median hourly earnings of the nonfarm self-employed.

These types of programs have an objective of providing recipients a minimum income level and/or standard of living.

All of these programs fall under the provisions of the World Trade Organization (WTO). The United States is a member of the WTO and has committed itself to limit its support to industry that affects the trade of goods and services. The WTO is the successor organization of the General Agreement on Tariffs and Trade (GATT). The GATT was established after World War II, along with agreements to form other international organizations, such as the World Bank and the International Monetary Fund. GATT provided rules on employment, restrictive government and business practices, investment, and world trade affairs. The Uruguay Round of Multinational Trade Negotiations replaced the GATT institutional framework with an official organization (the WTO) to oversee international trade issues.

There are sector-level trade agreements within the WTO. Agriculture is one of the sectors with such an agreement (often referred to as URAA for Uruguay Round Agreement on Agriculture). Under the URAA, countries agreed to reduce agricultural protection and support by opening domestic markets to import competition and by reducing domestic support and export subsidies. The market access provisions

prohibit new nontariff import barriers, convert existing nontariff barriers into tariffs, and specify a reduction in tariff levels. The export subsidy provisions prohibit new export subsidies and reduce both the level of export subsidies and the quantities exported under them. The domestic support provisions target reductions in trade-distorting domestic government policies.

The WTO commitments made by the United States are often cited as being an important constraint on the design of future U.S. farm programs. Indeed the counter-cyclical policy proposal made by the 21st Century Commission on Production Agriculture was designed to be "WTO compliant." But many are confused about the U.S. commitments and their future importance. The objective of this paper is to fill this gap in understanding by providing a detailed explanation of the WTO agreement and estimates of whether the United States has fully complied with its WTO commitments in recent years. In addition, we project the degree of compliance through the 2002 marketing year. After this projection, we examine new alternative program proposals to determine how they might impact U.S. compliance.

We find that the United States has met its WTO obligations in recent years. Furthermore, given no changes in the current policy mix, we project that the U.S. will continue to meet its commitments. However, some new policy proposals could jeopardize WTO compliance, particularly if WTO members adopt the recent U.S. proposal for stricter limits on agricultural support. The Proposal for Comprehensive Long-Term Agricultural Trade Reform, submitted to the WTO by the United States, outlines additional reductions in trade-distorting practices above existing guidelines.

## WTO Domestic Support Commitments

In the URAA, domestic support programs and policies are classified by their trade-distorting effects and their exemption status. The classifications are often described in terms of colored boxes: “green” for the least trade-distorting programs, “amber” for more trade-distorting programs, and “blue” for specific programs outlined in the agreement. Green and blue box programs are exempt from WTO commitments. Amber box programs may be exempt or may be limited under WTO commitments. The analogy of a traffic stoplight adequately describes the range of domestic support programs under the URAA. Countries can continue (“Go”) all green and blue box programs at any level of funding. Countries may continue to use amber box policies as long as the expenditures on them do not exceed set levels (“Proceed with caution”). Outlawed policies are placed in a “red” box (“Stop”).

The amber box expenditure limit is based on the country’s agricultural support over a base period. For the United States, the base period covers the years 1986 through 1988. The value of domestic support in the amber box is called the aggregate measure of support (AMS). The countries that signed the URAA agreed to limit amber box spending to a level at or below their AMS from their base period. Developed countries and confederations, such as the United States and the European Union, agreed to 20 percent reductions in their AMS limits by 1999. The U.S. base period AMS is \$23.9 billion. The current U.S. AMS limit is \$19.1 billion. Within the amber box, programs can be exempted from the limits if their AMS amounts are considered too small to count. These exemptions are referred to as *de minimis* exemptions.

The rules governing the placement of a domestic support program in the boxes are specific. Blue box policies are production-limiting policies that base payments on fixed yields and acreage. Payments must be limited to 85 percent of the base level of production. The old U.S. target price-deficiency payment program that existed before 1996 was a blue box program. Green box policies are policies that have minimal trade impacts. Payments from green box policies cannot be linked to current production and/or prices. The URAA lists several types of green box policies and the guidelines that must be followed. The following program types can qualify for the green box:

1. general services,
2. public stockholding for food security purposes,
3. domestic food aid,
4. direct payments to producers,
5. decoupled income support,
6. government financial participation in income insurance and income safety net programs,
7. payments for relief from natural disasters,
8. structural adjustment assistance provided through producer or resource retirement programs,
9. structural adjustment assistance provided through investment aids,
10. payments under environmental programs, and
11. payments under regional assistance programs.

Each of these program types has guidelines that define the eligibility of the program for the green box. Any direct payments to producers provided by a government program cannot involve transfers from consumers (only from taxpayers). Thus, green box programs cannot support

prices. The guidelines for decoupled income support are as follows:

1. eligibility for the program must be based on clearly defined criteria over a fixed base period;
2. payment amounts cannot be related to production, prices, or input usage after the base period; and
3. no production can be required to receive payments.

For government-provided income insurance or safety net programs to be green box, the requirements are as follows:

1. income and income loss can only be from agricultural sources;
2. loss must exceed 30 percent of average gross income (or an equivalent amount of net income) where average income is determined by a three-year average income (from the previous three years) or a five-year "olympic" average income (removing the high and low years before averaging); and
3. if payments are provided by this program and a natural disaster relief program, the total amount of payments cannot exceed 100 percent of the producer's total loss.

The requirements for natural disaster relief are as follows:

1. eligibility is determined by a formal disaster announcement from the government with at least a 30 percent production loss based on average production (the previous three-year average or the five-year "olympic" average);
2. payments may only be made on losses due to the disaster;
3. payments cannot be for more than the amount of loss and requirements for future production; and
4. if payments are provided by this program and a natural disaster relief program, the total amount of payments

cannot exceed 100 percent of the producer's total loss.

Producer retirement programs qualify for exemption if eligibility for the program is clearly defined on criteria to transition the producer out of agricultural production, and the payments are conditional on complete retirement from agricultural production. Resource retirement programs qualify under the following stipulations:

1. payments are conditional on the resource staying out of agricultural production for at least three years;
2. requirements cannot be placed on alternative use of the resource or other resources employed in agricultural production; and
3. payments cannot be related to any remaining agricultural production in which the producer is involved.

Environmental program payments qualify for the green box exemption if eligibility requirements are clearly defined and dependent on specific conditions, possibly involving production inputs or practices, and if the payment is limited to the extra cost or income loss the producer faces to be in compliance. Programs that fit these general types, but fail to meet the exemption conditions, and all other domestic support programs would fall into the amber box and would possibly be limited under the URAA.

Amber box policies can still be exempted from the AMS counted against a country's limit if the policy is termed *de minimis*. For developed countries, a 5 percent rule is used. For crop- or product-specific support, a policy can be declared *de minimis* if the expenditures under the policy are less than 5 percent of the value of production for the commodity. For non-crop- or non-product-specific support, all such policies can be declared *de minimis* if total



expenditures under all of the policies are less than 5 percent of the total value of agricultural production in the country.

### **What Boxes for Current Programs?**

The WTO agreements have had and will continue to have effects on U.S. farm policy. The 1996 farm bill and any future farm bills fall under the requirement of the URAA and any successor agreements. To see how current U.S. farm programs fare under the URAA, we examine the classification of U.S. farm programs and why the programs are classified as they are. Countries typically submit reports on overall domestic support two to three years after the fact. The United States has submitted reports for the 1995-1997 marketing years. For current policies that were in place at that time, we can place them in the WTO boxes based on these submissions. For current policies created after 1997, we will place the policies based on our interpretation of the URAA. Other interpretations are possible.

Current green box domestic support comes from several of the program types discussed in the previous section. General service programs include the Agricultural Research Service; the Tennessee Valley Authority; the Cooperative State Research, Extension, and Education Service; the Rural Business and Cooperative Development Service; the Animal and Plant Health Inspection Service; the Grain Inspection, Packers, and Stockyard Administration; the Food Safety Inspection Service; the Agricultural Marketing Service; the Economic Research Service; the National Agricultural Statistics Service; and the National Resource Conservation Service. These programs combined for nearly \$7 billion in domestic support in 1997. Domestic food aid accounted for nearly \$36 billion in 1997, with most of this total being in the food stamp and child nutrition programs.

PFC payments also are green box, as they are classified as decoupled income support. The construction of the PFC program follows the guidelines of a decoupled income support program that qualifies for exemption. Payment eligibility and amounts are based on historical production over a base period. Current production decisions (even the decision not to produce at all) cannot affect the payment. Given that there is no link between current production and PFC payments, these payments should have no effect on future production and therefore are not trade distorting.

Green box natural disaster relief programs include the Non-insured Crop Disaster Assistance Program, the Livestock Indemnity Program, and emergency feed and forage programs. The Conservation Reserve Program qualifies as a resource retirement program. Programs that facilitate structural adjustment through investment aids include the Farm Credit Program and State Mediation Grants. Environmental programs that qualify for exemption include the Agricultural and Emergency Conservation Programs, the Great Plains Conservation Program, the Water Bank Program, the Wetland Reserve Program, and the Environmental Quality Incentives Program.

The United States has increased its green box spending by a large amount over the past several years. Over the period 1986-1988, total expenditures for programs that would have qualified for the green box were, on average, just over \$26 billion. In 1996 and 1997, green box spending increased to over \$51 billion. Because the green box spending is exempt from WTO limits, the United States can continue to add to this total.

It is in amber box spending that the United States could run afoul of the WTO and the URAA. Amber box spending is lim-

ited under the URAA, and the United States, as a developed country, has agreed to reduce such spending by 20 percent from its 1986-1988 average. This implies that the United States can spend up to \$19.1 billion on amber box programs. Figure 2 shows the AMS limits, actual AMS amounts for 1996 and 1997, and our projections for AMS amounts for 1998 to 2002. Our projections are based on USDA figures on various program expenditures for 1998-2001, where possible, and USDA and Food and Agricultural Policy Research Institute (FAPRI) projections for 2002 figures when actual data could not be obtained.

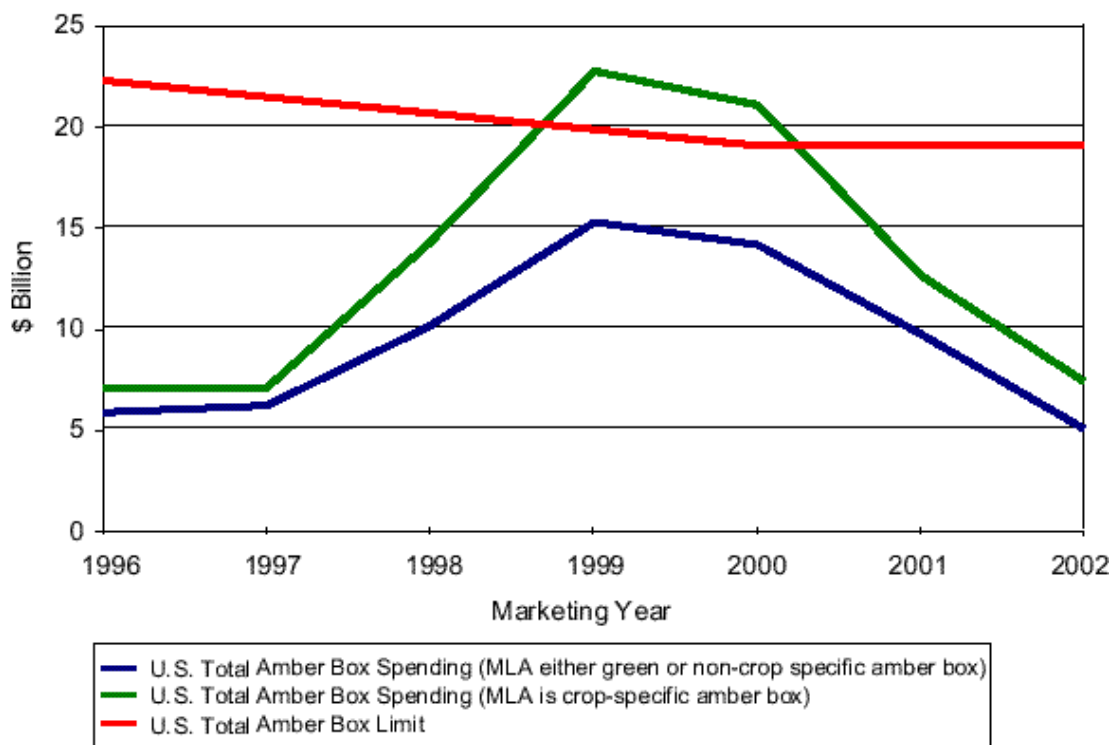
AMS is separated into product-specific and non-product-specific categories for the calculation of *de minimis* exemptions. In 1996 and 1997, the United States reported the following program payments or costs as product-specific domestic support: the dairy, sugar, and peanut price support/quota programs; marketing loan gains; loan deficiency payments; commodity loan forfeiture costs; cotton user marketing payments; dairy indemnities; mohair and wool support payments; rice marketing certificate payments; tobacco price related payments; commodity storage payments; and commodity loan interest subsidies. Over the same time period, the United States reported these non-product-specific domestic support payments: estimated water subsidies from several Bureau of Reclamation projects, net federal outlays for livestock grazing on federal land, net crop insurance indemnities (insurance payments less producer-paid premiums) for both yield and revenue insurance policies, and state credit programs.

Marketing loan gains, loan deficiency payments, commodity storage payments, and commodity loan interest subsidies arise from the marketing loan programs. The price support and marketing loan program expenditures are classified as amber box

because payments depend on current production and prices. Given this link, the programs can influence future production decisions and have trade-distorting effects. Net crop insurance indemnities are also in the amber box because they do not meet the green box requirements. The yield and revenue insurance policies are not income insurance policies; coverage above 70 percent is allowed; and the government does not have to declare a disaster for payments to begin. Thus, this insurance cannot qualify as green box either as an income safety net program or as a natural disaster relief program.

Over the last three years, the federal government has augmented agricultural spending with emergency assistance packages. These packages included market loss assistance (MLA) and crop loss assistance payments for several commodities. The crop loss assistance payments were constructed to follow the guidelines for a natural disaster relief program and are exempt from WTO limits (that is, they are green box). The market loss assistance payments follow the same payment formula as the PFC payment (which are green box), but the justification for the payments was the low market prices we have seen over the last few years. Therefore, we assume that the market loss assistance payments fall into the amber box because the payments were triggered by (then) current market prices. The payment structure of the market loss assistance programs is non-product-specific because current production has no impact on the payments.

Other arguments could lead to the market loss assistance payments being classified differently. Because the payment rates are crop-specific, it could be argued that the MLA payments are product-specific (but still within the amber box). Under this scenario, the MLA payments for each crop would be compared to the value of the individual crops rather than to the total value of agricultural



Note: Actual numbers are reported for 1996 and 1997. Projections are made for 1998 and beyond.

**FIGURE 2. Total amber box spending, payment caps, and *de minimis* exclusions**

production. This classification would lead to higher AMS amounts for the United States, adding enough to the AMS total to exceed the limits in 1999 and 2000. It could also be argued that PFC payments (green box) and MLA payments should be classified the same way. There is no formula linking the MLA payments to current market prices. Any link from the MLA payments to current prices is derived from interpreting the intent of the U.S. Congress. If this argument held, then the MLA payments would be classified as green box and would be exempt from the WTO limits in the URAA. The main difference, as far as AMS amounts, between this classification and the one we assume is that the MLA payments could count toward the AMS limits under our assumptions, but they could not count if they are considered green box. This shows that even with the specific guidelines

in the URAA, arguments can be made to place the same program in different boxes.

Table 1 displays the actual and projected values of production used in this analysis. The overall value of agricultural production has fallen since 1996. By 1999, the value of agricultural production had dropped to \$183 billion, nearly \$23 billion less than the 1996 value. The projections indicate that production values have increased and will continue to do so. By 2002, agricultural production will be valued at \$199 billion. These production values affect the U.S. WTO standing as they are used to evaluate U.S. domestic support versus the AMS limit. The *de minimis* exemptions are determined by comparing domestic support against 5 percent of the production value.

**TABLE 1. Value of production**

Commodity	1996	1997	1998	1999	2000	2001	2002
	(\$ Billion)						
Barley	1,091	862	687	553	632	740	760
Beef and Veal	22,259	24,893	24,153	25,961	29,175	30,436	30,715
Corn	25,312	22,352	18,922	17,950	18,621	19,930	20,895
Cottonseed	915	835	687	562	677	683	676
Cotton	6,408	5,976	4,120	3,836	4,781	4,962	4,872
Dairy	23,057	21,191	24,520	23,602	20,889	21,536	20,730
Honey	180	148	147	125	151	151	151
Canola	62	88	160	107	135	138	140
Flaxseed	10	14	34	31	35	36	37
Mustard	2	9	11	5	4	4	4
Rapeseed	0	0	1	0	1	1	1
Safflower	76	60	58	55	30	30	31
Sunflower	418	427	537	353	241	246	250
Mohair	15	15	13	10	11	14	14
Oats	319	273	200	170	165	160	156
Peanut	1,030	1,003	1,126	992	845	1,012	1,028
Rice	1,687	1,756	1,687	1,257	1,073	1,239	1,339
Rye	33	30	30	25	21	23	24
Sorghum	2,004	1,409	905	971	823	1,038	1,060
Soybean	17,455	17,373	13,494	12,451	13,073	13,345	13,543
Sugar	2,044	2,050	2,242	2,092	2,179	2,204	2,120
Tobacco	2,852	3,217	2,701	2,329	2,056	1,512	1,920
Wheat	9,815	8,287	6,781	5,904	5,970	6,345	6,609
Wool	40	45	29	18	15	32	32
All Other Commodities	88,614	91,571	87,746	83,947	89,783	91,908	92,229
<b>Total</b>	<b>205,701</b>	<b>203,884</b>	<b>190,991</b>	<b>183,309</b>	<b>191,387</b>	<b>197,726</b>	<b>199,336</b>

Table 2 shows all of the amber box expenditures before the de minimis exemptions are taken. These figures represent all possible expenditures that could count against the WTO limits. In 1996 and 1997, over \$7 billion was spent on amber box programs. As prices deteriorated, marketing loan expenditures (loan deficiency payments, marketing loan gains, and commodity loan interest subsidies) grew. Market loss assistance payments were also appropriated. Thus, in 1998, amber box spending rose to \$14 billion. In 1999 and 2000, spending rose to over

\$21 billion. With projections of stronger prices and no additional market loss assistance, total amber box outlays are expected to fall to under \$13 billion in 2001. By 2002, changes in the dairy programs are scheduled to take effect and reinforce the decline in spending. Outlays are projected to fall to \$7 billion in 2002.

Table 3 shows the expenditures that count against the U.S. AMS limit. The de minimis exemptions offset a sizable portion of the increase in amber box spending. In

**TABLE 2. Aggregate measures of support (before *de minimis* exemptions)**

Commodity	1996	1997	1998	1999	2000	2001	2002
	(\$ billion)						
Barley	1	4	85	40	69	26	34
Beef and Veal	0	0	0	0	0	0	0
Corn	28	150	1,557	2,541	2,416	520	0
Cottonseed	0	0	0	79	100	0	0
Cotton	3	466	867	2,033	465	264	170
Dairy	4,691	4,456	4,431	4,253	4,931	4,318	1
Honey	0	0	0	0	0	0	0
Canola	0	0	9	39	77	92	90
Flaxseed	0	0	2	11	23	28	28
Mustard	0	0	0	1	0	0	0
Rapeseed	0	0	0	0	0	0	0
Safflower	0	0	0	2	1	0	0
Sunflower	0	0	23	141	138	160	157
Mohair	0	0	1	0	6	10	0
Oats	0	0	20	29	42	34	14
Peanut	299	306	264	322	330	268	267
Rice	6	6	42	438	440	573	542
Rye	0	0	0	0	0	0	0
Sorghum	1	2	63	154	82	13	0
Soybean	14	45	1,317	2,845	2,817	2,971	2,917
Sugar	908	1,012	1,052	1,136	1,060	1,022	1,042
Tobacco	-6	18	3	330	342	1	2
Wheat	8	36	527	958	848	130	61
Wool	0	0	0	0	5	10	0
Non-Product-Specific	1,115	563	4,010	7,451	6,954	2,219	2,124
<b>Total</b>	<b>7,068</b>	<b>7,064</b>	<b>14,271</b>	<b>22,802</b>	<b>21,148</b>	<b>12,659</b>	<b>7,447</b>

1996 and 1997, the U.S. AMS was roughly \$6 billion, with most of this support going to dairy producers. Only three products received enough support in 1996 to exceed the *de minimis* exemption level. By 1999, 17 products had support exceeding the *de minimis* exemption level, and the AMS had risen to over \$15 billion. This amounts to 75 percent of the U.S. AMS limit. If the market loss assistance had counted as product-specific,

the United States would have exceeded the AMS limit in 1999 and 2000. For 2001 and 2002, because prices are projected to rise, so do production values and *de minimis* exemption limits. This means that more spending could qualify for exemption. But increasing prices also implies smaller marketing loan outlays and reduced amber box spending. By 2002, the U.S. AMS is projected to fall to nearly \$5 billion.

**TABLE 3. Aggregate measures of support (after *de minimis* exemptions)**

Commodity	1996	1997	1998	1999	2000	2001	2002
	(\$ billion)						
Barley	0	0	85	40	69	0	0
Beef and Veal	0	0	0	0	0	0	0
Corn	0	0	1,557	2,541	2,416	0	0
Cottonseed	0	0	0	79	100	0	0
Cotton	0	466	867	2,033	465	264	0
Dairy	4,691	4,456	4,431	4,253	4,931	4,318	0
Honey	0	0	0	0	0	0	0
Canola	0	0	9	39	77	92	90
Flaxseed	0	0	2	11	23	28	28
Mustard	0	0	0	1	0	0	0
Rapeseed	0	0	0	0	0	0	0
Safflower	0	0	0	0	0	0	0
Sunflower	0	0	0	141	138	160	157
Mohair	0	0	0	0	6	10	0
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Rye	0	0	0	0	0	0	0
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Soybean	0	0	1,317	2,845	2,817	2,971	2,917
Sugar	908	1,012	1,052	1,136	1,060	1,022	1,042
Tobacco	0	0	0	330	342	0	0
Wheat	0	0	527	958	848	0	0
Wool	0	0	0	0	5	10	0
Non-Product-Specific	0	0	0	0	0	0	0
<b>Total</b>	<b>5,898</b>	<b>6,238</b>	<b>10,193</b>	<b>15,350</b>	<b>14,192</b>	<b>9,751</b>	<b>5,055</b>

### What Box for Proposed Programs?

Adjustments to the farm bill will need to be examined to see where they fit within the URAA and to fully consider their impact on the U.S. AMS. Policies that increase or rebalance the marketing loan rates may change programs that are already marked as product-specific amber box spending. Given the price projections for 2001 and 2002, these changes would likely lead to a higher AMS and push the United States even closer to its AMS limit. The flexible fallow program would also

be considered product-specific amber box spending, even though it has production-limiting features (like blue box programs) because the payments are triggered by current prices and are not limited to 85 percent or less of some base level of production.

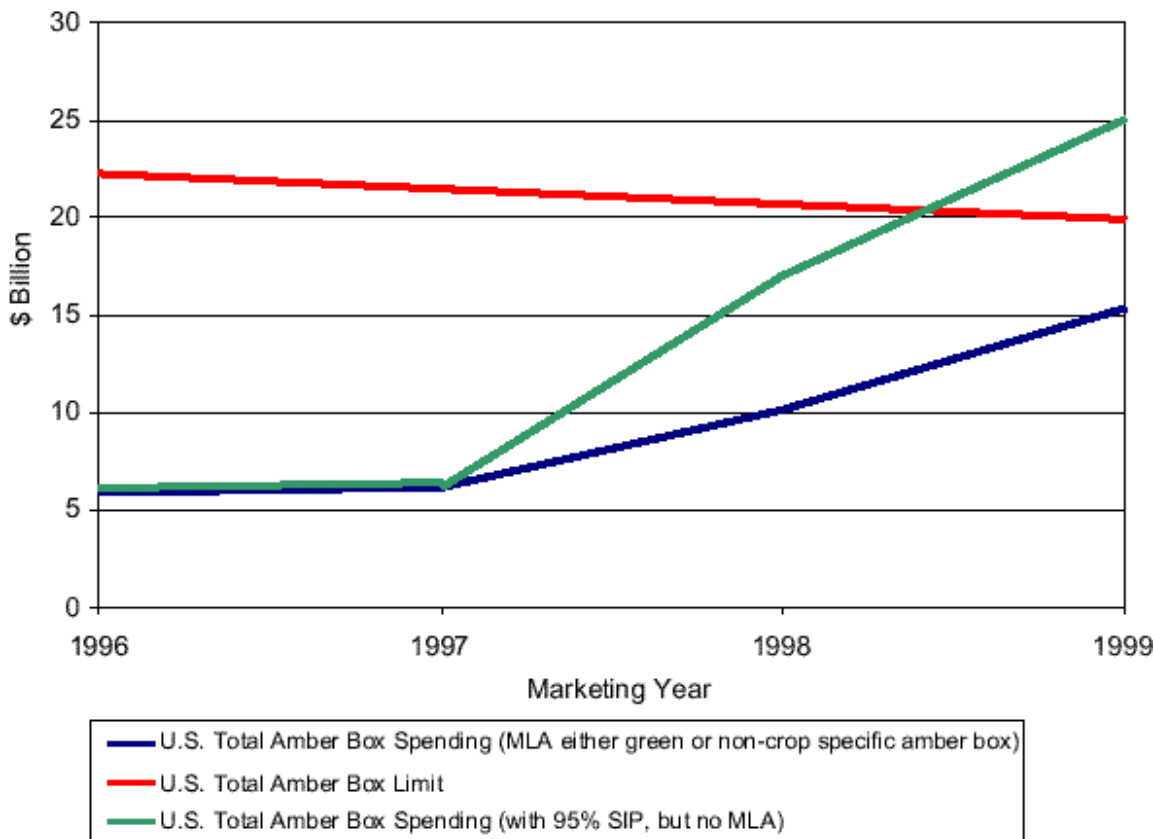
The SIP and SIAP proposals are product-specific amber box programs because payments are triggered by shortfalls in current prices or production. The Commission on 21st Century Production Agriculture's countercyclical proposal is non-product-specific, as it looks at income across eight

crops. But our interpretation of the URAA indicates that it also would be considered amber box because current prices and production from the eight crops are used to determine the overall amount of payments. In fact, the URAA guidelines for the exemption of decoupled income support exclude any countercyclical program based on current prices or production.

New policies that include environmental payments could also fall into the amber box if the payment exceeds the additional cost or loss of income that producers face in implementing the requirements of the program. The farm income safety net programs, examined by the USDA, would fail to qualify for the green box. The guidelines for income safety net programs explicitly outline the

income levels that can be supported and the distribution of the payments. None of the income programs follow this outline.

Most current proposals keep the existing marketing loan, crop insurance, and PFC programs in place. This implies that any additional expenditures from these proposals would add to the U.S. amber box spending and possibly to the U.S. AMS (barring *de minimis* exemptions). Therefore, the probability that the U.S. will exceed its WTO domestic support limit increases under these proposals. For example, if the SIP proposal with a 95 percent coverage level had been in place instead of the Market Loss Assistance payments, then the United States would have exceeded the amber box spending caps. Figure 3 shows the estimated payments and



Note: Actual numbers are reported for 1996 and 1997. Projections are made for 1998 and beyond.

**FIGURE 3. Total amber box spending with a 95 percent SIP program**

the extent to which we would have exceeded the limits.

As the URAA now stands, the goal of having a new countercyclical farm program conflicts with the goal of reducing trade-distorting policies. Most variations on a countercyclical farm program would fail to qualify for a green box exemption due to their very nature. After all, how can a program be countercyclical if it cannot be based on current prices and yields? Efforts to construct a countercyclical farm program that is green box would require a redefinition of the meaning of "countercyclical." Adding a new amber box countercyclical program might require the elimination of one or more existing policies. Such a move could be justified because both the price support programs and the crop insurance programs provide countercyclical support. A new program could, depending on its design, substitute quite effectively for either program (Hart and Babcock).

### **Concluding Comments**

In June of 2000, the United States proposed an extension to the URAA that builds on its reform measures. The proposal would simplify the policy classifications, narrowing them to two: exempt and nonexempt policies. AMS levels would again be reduced, with the final level determined by a fixed percentage of the country's total value of agricultural production in a fixed base period. The percentage would be the same for

all participating countries. Exemption requirements would be rewritten to emphasize the limiting of trade-distorting practices. Criteria for the exemption of programs essential to food security and development in developing countries would be added.

The reasoning behind this proposal is that it is both in our national and global interest to expand agricultural trade. By removing trade-distorting domestic support policies, countries are allowing agricultural producers to base production decisions on market and environmental signals. This will expand economic opportunity for the agricultural sectors while addressing food security and environmental concerns. Consumers will also benefit through more competitive prices and a wider array of products.

This official stance of U.S. trade negotiators clearly is not shared by U.S. domestic concerns whose advocates propose to significantly expand U.S. support for agriculture. Much of the proposed support would count against the WTO commitments made by the United States. A clear understanding of what those obligations are and how new policy proposals fit into the WTO framework is critical for all concerned as the United States tries to revamp its farm programs while maintaining its overall commitment to expanded trade.



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