

World Agriculture & Trade



Aligning U.S. Farm Policy With World Trade Commitments

Farm income support and trade programs will probably continue to be subject to restrictions established under international trade agreements. The U.S. and other countries made commitments in 1994 under the Uruguay Round Agreement on Agriculture (URAA) to reduce the total amount of trade-distorting domestic subsidies provided to producers, to reduce export subsidies, and to increase import access to domestic markets. The implementation period for the commitments was 1995 to 2000, and existing commitments will continue at 2000 levels until a new agricultural trade agreement is reached under the new multilateral trade negotiations initiated in Doha, Qatar, on November 15, 2001.

The U.S. has so far met commitments under the URAA, but surges in direct payments to producers after 1997 in response to low market prices have raised concerns that domestic subsidy levels might eventually exceed the ceiling on domestic support established under the URAA. U.S. support is expected to remain below its ceiling under current farm programs, but increases in support under new programs could cause a compliance problem with the URAA commitments. A compliance problem could hamper efforts in the new multilateral trade talks to accomplish U.S.

goals for liberalizing international trade and getting other countries to reduce domestic support to their agriculture sectors and increase market access. Support can be provided without affecting compliance, however, if programs are designed to be consistent with certain URAA exemption provisions.

How Compliance Is Determined

Domestic subsidies under the URAA are measured using a specially defined indicator, the "aggregate measurement of support" (AMS). In 1994, 28 countries established ceiling levels for their AMS and agreed to reduce them by 20 percent by the year 2000. Countries must document in official notifications to the World Trade Organization (WTO), the governing body for the URAA, their calculated AMS for each year, 1995 to 2000. The U.S. has, so far, officially notified for marketing years 1995 to 1998. Information for 1999 and 2000 is under internal review for later notification.

Domestic support to agriculture is classified into three basic categories for purposes of AMS calculations and WTO notifications:

Green box support is the least trade distorting. As such, it is exempt from support reduction commitments and thus not included in the AMS. This category includes certain types of support received directly by producers in the form of government payments or input subsidies, as well as certain government outlays not received directly by producers, but that provide benefits to the agricultural sector in general. Three types of green box support of particular interest to lawmakers drafting new farm legislation are decoupled income support (i.e., support not tied to current production level or current market prices), income insurance and safety-net payments, and environmental payments.

Blue box support has supply-control features that partially offset trade-distorting effects, and is also exempt from inclusion in the AMS. The U.S. currently makes no direct payments to farmers that fit into this category. U.S. deficiency payments were linked to compliance with acreage reduction programs prior to 1996, so they were in the blue box in 1995. Deficiency payments were eliminated after 1995 under the 1996 Farm Act.

Amber box support is the most trade-distorting type. It includes all direct support to agriculture that is not eligible for the green or blue boxes. All amber box subsidies must be included in the AMS calculation, except those qualifying for what is known as the *de minimis* exemption. This exemption permits product-specific support to be excluded from the AMS if the product's total support does not exceed 5 percent of its value of production (10 percent for developing countries). Also, non-product-specific support, e.g., input subsidies and direct payments not related to current production of specific commodities, can be excluded from the AMS if the total value is less than 5 percent of the total value of all agricultural commodities produced (10 percent in the case of developing countries).

Examples of the largest amber box support included in the U.S. AMS in 1998 were market price support benefits for dairy and sugar, and benefits related to marketing assistance loans, especially loan deficiency payments.

Total domestic support to agriculture can be defined to include all the benefit measures included in the above three boxes, before any exemptions and regardless of the *de minimis* status. However, the remainder of this article focuses only on the support measures received directly by producers, called “total direct support to agricultural producers,” or simply “total direct support.”

This total includes all of the amber box and blue box support measures plus green box outlays that involved payments made directly to producers. This total therefore excludes green box outlays notified to the WTO as domestic food aid and outlays for general government services such as research, inspection, and marketing. These latter items must be notified to the WTO but do not involve direct payments to producers.

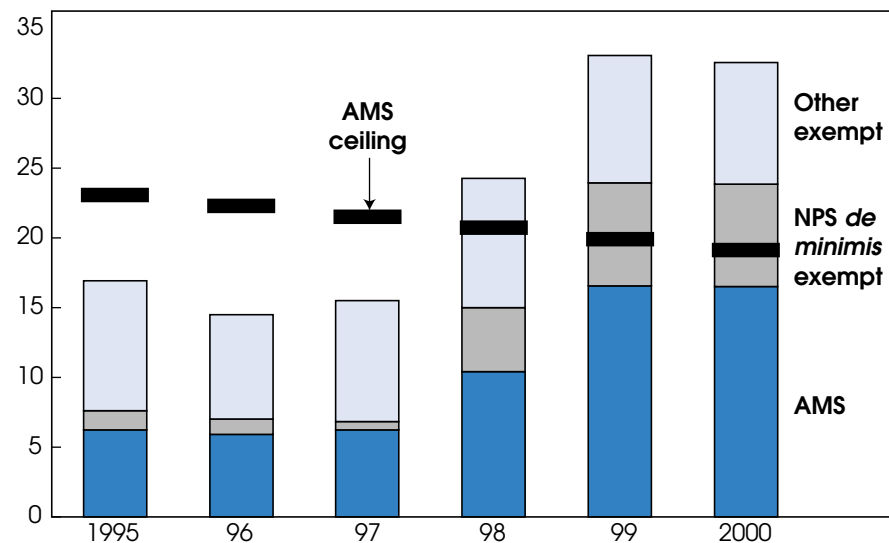
Total direct support to U.S. agricultural producers before subtracting the exempt blue, green, and *de minimis* payments was less than the AMS ceiling in 1995-97. Direct payments increased enough after 1997 to cause total direct support to exceed the AMS ceiling each year, making the exemptions essential to meeting URAA commitments.

The U.S. AMS in 1998 was \$10.4 billion, just 50 percent of the \$20.7-billion ceiling. Preliminary estimates for 1999 and 2000 indicate that the average AMS during these years was nearly 60 percent higher than in 1998. This means the AMS for these years would now be much closer to the ceiling, perhaps as much as 80 percent.

This increase in the AMS reflects primarily the larger loan deficiency payments and marketing loan gains received by producers as a result of low market prices relative to commodity loan rates. There were also increases in the AMS due to payments related to emergency programs for various commodities. The implication for lawmakers is that some future programs may need to be carefully crafted to assure they fall into an exempt category in order to keep the AMS within the ceiling.

Total Direct Support Reported to the WTO— U.S. AMS Approaches the Ceiling

\$ billion



AMS (aggregate measurement of support) is the actual U.S. direct support to farmers minus exemptions allowed by the World Trade Organization (WTO). 1999 and 2000 estimates are from *Food and Agricultural Policy: Taking Stock for the New Century*, USDA.

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Criteria for Green Box Inclusion

For support programs to qualify for the green box category, and thus be exempt from the AMS, they must meet both general and policy-specific criteria. Under the general criteria, support provided by the program:

- shall be provided by a publicly-funded government program and not involve transfers from consumers,
- shall not have the effect of providing price support to producers, and
- shall have no, or at most minimal, trade-distorting effects on production (this criterion is subject to considerable interpretation since “minimal” is not defined).

Green box provisions do not set any upper constraints on the total amount of green box support that can be given to agriculture. The three largest direct payment categories in the U.S. green box in 1998 (in value terms) were decoupled income support (production flexibility contract payments), resource retirement payments (Conservation Reserve Program pay-

ments), and payments for natural disasters (crop and livestock disaster payments).

Decoupled income support. Direct payments to producers are considered decoupled payments if they are not related to or based on market prices, the type or volume of production, or factors of production in any year after a defined and fixed base period. The U.S. included production flexibility contract (PFC) payments as decoupled payments in the 1996-98 notifications to the WTO. These payments were the largest single category value-wise, representing 23 percent of total direct payments to producers in 1998.

The PFC totals were largely predetermined by the 1996 Farm Act using acreage and program yields that would have been in effect for 1996 under previous legislation. Current prices, resource use, and production decisions did not affect the amount of PFC payments received by a farmer under the 1996 Act unless PFC land was used for nonfarm purposes or for producing fruits and vegetables. Consequently, one may argue, current production decisions and cropping patterns are not significantly distorted by current PFC payments. There may be

World Agriculture & Trade

U.S. Direct Support to Agricultural Producers in 1998 Notified to WTO

WTO category	Qualifying U.S. program or payment name	1998 total amount	AMS exempt	1998 AMS ¹
<i>\$ billion</i>				
Amber box support				
Product-specific-- (exempt from AMS when support for a commodity does not exceed 5% of commodity's total value of production)	Dairy market price support	4.33	0.00	4.33
	Loan deficiency payments	2.78	0.01	2.77
	Sugar market price support	1.09	0.00	1.09
	Marketing loan gains	1.04	0.02	1.02
	Peanut market price support	0.35	0.00	0.35
	Commodity loan interest subsidies	0.34	0.00	0.34
	All other product specific, less fees	0.61	0.08	0.53
	Subtotal	10.55	0.16	10.39
Nonproduct-specific-- (exempt from AMS when subtotal does not exceed 5% of total value of agricultural products for the year)	Crop market loss payments	2.81	2.81	0.00
	Crop and revenue insurance benefits	0.75	0.75	0.00
	All other	1.03	1.03	0.00
	Subtotal	4.58	4.58	0.00
Blue box support (AMS exempt)				
	Deficiency payments (ended in 1995)	0.00	0.00	0.00
	Subtotal	0.00	0.00	0.00
Green box support² (AMS exempt)				
Decoupled income support	Production flexibility contract payments	5.66	5.66	0.00
Resource retirement payments ³	Conservation Reserve Program payments	1.69	1.69	0.00
Relief from natural disasters	Payments for crop disaster, non-insured assistance program, and other crop, livestock, and tree disaster assistance and subsidized loans	1.41	1.41	0.00
Environmental program payments ³	Program payments for wetland reserve, environmental quality incentives, emergency conservation, and other environmental and conservation programs	0.26	0.26	0.00
Structural adjustment investment aids	Farm credit programs	0.09	0.09	0.00
All other payments to producers		0.00	0.00	0.00
	Subtotal	9.11	9.11	0.00
Total direct support to producers		24.24	13.85	10.39
WTO ceiling		Na	Na	20.70
Excess of WTO ceiling over the AMS		Na	Na	10.30

Na = Not applicable. WTO = World Trade Organization. AMS = Aggregate measurement of support.

1. Excludes the blue and green box entries, and any amber box amounts that are exempt under the 5 percent *de minimis* rule. 2. In this article, green box excludes outlays notified to the WTO as green box outlays not received directly by producers, such as domestic food aid and general government services (research, inspection, marketing, and other services). 3. Revised to exclude technical assistance.

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longrun effects on production, however, since PFC payments increase the business income of farm families no matter what they produce, even if they completely idle their PFC land.

A key issue arising from farm bill proposals for income safety nets, or counter-cyclical payments, concerns the interpretation of the URAA condition stating that decoupled payments must not be based on or related to market prices in any year after the base period. Payments in many income safety-net program proposals are triggered by variations in commodity revenue or farm income. Since revenue and income are related to prices, such payments would have to be carefully crafted

to qualify as "decoupled" income support. If the payments do not qualify as decoupled income support, could they qualify for the green box under income insurance provisions?

Income insurance and income safety nets. Direct payments to producers can be considered income insurance or safety-net payments under the green box category if they meet four policy-specific criteria:

- eligible producers must have experienced a loss that exceeds 30 percent of average gross income, or the equivalent in net income terms, during the preceding 3-5 year period;

- the amount of current payments must not exceed 70 percent of the current income loss;
- payments shall relate solely to income, and not to prices, production, or factor use; and
- payments from this provision combined with that for natural disaster relief shall not total more than 100 percent of the total loss for individual farmers.

The U.S. green box does not currently include any programs based on the above safety-net criteria, but some farm bill proposals for income safety nets seemed similar in concept to green box income insurance. Whether or not these proposals, if

World Agriculture & Trade

adopted, would actually qualify for any green box category has yet to be determined. The language of the URAA provisions for income insurance contains some ambiguities and significant benefit limitations. In 1995-98, U.S. income and revenue insurance benefits were combined with multiperil crop insurance benefits and notified to the WTO as nonproduct-specific, amber box support.

URAA income insurance provisions cover programs that make payments to producers based on their unique individual income experiences. Income insurance or safety-net programs, such as those in some farm bill proposals that base payments on national-level indicators, would not qualify for the income insurance category of the green box. If they were not carefully crafted to qualify for the green box as decoupled payments, they would probably have to be included in the amber box and could make it harder for the U.S. to remain within its AMS ceiling.

Environmental program payments.

Direct payments to producers under environmental programs qualify as green box payments if they require producers to meet clearly defined specific conditions related to production methods or inputs. The amount of the payments shall be limited to the extra cost or loss of income from complying with such conditions. U.S. funding for environmental programs in the green box category has been relatively small compared to total farm program spending, but some farm bill proposals called for increasing such outlays.

The green box condition that limits the amount of payments to the cost of compliance might be an issue for policymakers to consider. Payments to landowners under the U.S. Conservation Reserve Program (CRP) have been notified in the green box under the resource retirement rather than environmental programs category.

Resource retirement payments. Payments made conditional on retirement of land from marketable agricultural production for at least 3 years may be placed in the green box category called “structural adjustment assistance provided through resource retirement programs.” Such payments cannot be related to current prices, type or quantity of production, or

to remaining resources. To qualify as green box, a program also cannot require that the retired resources be used for any alternative production of marketable agricultural products. In 1998, the CRP was listed as a resource retirement program in the U.S. green box. The CRP, which would be expanded under farm bill proposals, was the fifth-largest component of total direct support to U.S. agricultural producers in 1998.

Other green box programs. The third-largest green box category that involved direct payments in 1998 was payments to farmers for relief from natural disasters—accounting for \$1.4 billion in support provided in response to widespread weather-related crop damage. A small amount of U.S. farm credit subsidy was notified in the category for “structural adjustment payments involving investment aids” (interest rate subsidies). The U.S. reported nothing in the other direct payment categories of the green box—those for producer retirement or regional assistance payments.

Amber Box Support Exclusions

The U.S. included several programs in the amber box nonproduct-specific (NPS) category of support since they were multi-product in scope, the implementation provisions were generic, or the payment amount was not based on current production of any specific commodity. (The URAA does not define “nonproduct spe-

cific”). Since the total value of the NPS category of payments for the U.S. was \$4.6 billion in 1998, or only 2.4 percent of total value of production (and thus below the 5 percent *de minimis* level for developed countries), the entire \$4.6 billion was excluded from the U.S. AMS. The largest two examples of NPS support in the U.S. in 1998 were the crop market loss payments and the net benefits from crop and revenue insurance.

Crop market loss assistance payments.

Producers who received fiscal 1998 PFC payments also received additional payments allocated to producers in proportion to the amount of their PFC. These additional payments, called crop market loss payments, were mandated by legislation enacted in October 1998 partly in response to generally low agricultural market prices. The payments were not tied to current production of any specific product, and the proportionality factor was the same (generic) for each PFC commodity. But since payments were based on or related to recent market-price conditions, they could not be classified as green box decoupled payments. Crop year 1998 payments amounted to \$2.8 billion.

Crop and revenue insurance benefits.

Insurance benefits were measured as the amount of insurance indemnities paid to producers, minus the producers’ share of the insurance premiums. Producers are offered generic, or common, provisions for participation in various insurance programs operated by USDA’s Risk Manage-

Find more information on the Economic Research Service website

Food and Agricultural Policy—Taking Stock for the New Century

www.usda.gov/news/pubs/farmpolicy01/fpindex.htm

WTO: Uruguay Round Agreement on Agriculture—Domestic Support

(World Trade Organization Briefing Room)

www.ers.usda.gov/briefing/WTO/domsupport.htm

U.S. Ag Policy—Well Below WTO Ceilings on Domestic Support

(Agricultural Outlook)

www.ers.usda.gov/publications/agoutlook/oct1997/ao245h.pdf

U.S. WTO Domestic Support Reduction Commitments and Notifications

(Farm and Commodity Policy Briefing Room)

www.ers.usda.gov/briefing/farmpolicy/usnotify.htm

U.S. Farm Program Benefits: Links to Planting Decisions and Agricultural Markets

(Agricultural Outlook)

www.ers.usda.gov/publications/agoutlook/oct2000/ao275e.pdf

World Agriculture & Trade

ment Agency. The Federal government subsidizes the insurance premium. Taken as a whole, insurance program provisions do not comply with all the green box provisions for payment for relief from natural disasters, which includes qualifying crop insurance programs. In particular, the requirement for the green box that recipients of crop and revenue insurance payments must have at least a 30-percent loss is not always met. Crop-year net insurance payments amounted to \$747 million in 1998.

Other NPS programs. Other NPS benefits notified to the WTO include input subsidies (for irrigation, grazing livestock, and state credit programs) and 1998 multiyear disaster payments. This disaster payment program did not fully comply with the 30-percent loss threshold criteria for disaster relief in the green box, so it was notified in the amber box as NPS, since the provisions are generic, or common provisions, similar to crop insurance. The input subsidies are clearly not limited to any specific products.

U.S. Farm Support At a Crossroads

As the U.S. enters the 21st century, many policymakers are struggling to reshape the nature of U.S. agricultural policy. Significant public interest in market-oriented policy, environmental policy, and URAA commitments is encouraging the development of “decoupled” income support programs, safety-net and risk management tools, and environmentally focused incentives. Programs with payments tied to current levels of production, prices, or resource use are limited under the URAA.

Thus far, the U.S. has been able to comply with the conditions established by its URAA commitments and still provide significant income support to producers. U.S. support under current farm programs is expected to remain below its ceiling, but any increases in support under new programs, if not carefully crafted to utilize exemptions, could present a problem for compliance with the URAA commitments. **AO**

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Upcoming Reports—USDA's Economic Research Service

The following reports are issued electronically at the times indicated.

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February

- 8** *World Agricultural Supply and Demand Estimates*
(8:30 a.m.)
- 11** *Oil Crops Outlook* (4 p.m.)**
Cotton and Wool Outlook
(4 p.m.)**
Rice Outlook (4 p.m.)**
- 12** *Wheat Outlook* (9 a.m.)**
Feed Outlook (9 a.m.)**
- 13** *Livestock, Dairy, and Poultry
Situation and Outlook* (4 p.m.)
- 20** *Vegetables and Melons
Outlook* (4 p.m.)
Agricultural Outlook (3 p.m.)*
- 21** *Outlook for U.S. Agricultural
Trade* (4 p.m.)
- 25** *U.S. Agricultural Trade Update*
(4 p.m.)
- 26** *Agricultural Income and
Finance Situation and
Outlook* (4 p.m.)*

*Release of summary.

**Available electronically only.

What's ahead in 2002

- * Calculating trade damages in WTO disputes
- * Report on farm labor
- * Issues in animal waste disposal
- * The economics of farmland protection
- * Intellectual property rights: the impact on global agriculture

All in upcoming issues of *Agricultural Outlook*