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**Commodity Support in the 2008 Farm Bill and the Doha Round**

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## **Abstract**

The US agriculture policy, mainly in the form of a farm bill, is closely related to multilateral trade talks. The whole developing world is seriously dissatisfied with the long-standing subsidies in the US agricultural policy, and expects the US to undertake reforms, particularly on the commodity support in the farm bill, with a view to pushing forward the on-going Doha negotiations. However, in spite of minor changes in the commodity programs, the 2008 Farm Bill generally continues with the farm commodity price and income support framework of the previous legislation.

The US subsidy program has already been under scrutiny within the international trade arena, and whether the US violates its WTO commitment depends on how it will notify the commodity programs. The US is in a defensive position in the on-going Doha agriculture negotiation on the reduction of trade-distorting domestic support. However, the impact of the possible Doha deal on the implementation of the 2008 Farm Bill remains to be seen in the future. In addition, even though the US farm legislation in some way led to the failure of the recent ministerial conference in Geneva, it could turn out to be a building block for the negotiations. Furthermore, for developing country governments such as China, the government authorities need to weigh carefully the political and economic benefits and cost of suing the US subsidy before the WTO Dispute Settlement Body.

Note: The views expressed in this paper are those of the author only and do not necessarily reflect the views of the author's employer.

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## Acronyms and Abbreviations

ACRE	Average Crop Revenue Election Program
AAGI	Average Adjusted Gross Income
AMS	Aggregate Measures of Support
AoA	Agreement on Agriculture
ASCM	Agreement on Subsidies and Countervailing Measures
CoA	Committee on Agriculture, WTO
CCPs	Counter-Cyclical Payments
DDA	Doha Development Agenda
DSB	Dispute Settlement Body
EU	European Union
FCEA	The Food, Conservation, and Energy Act of 2008
GATT	General Agreement on Tariffs and Trade
LDPs	Loan Deficiency Programs
MALs	Marketing Assistance Loans
MOFCOM	Ministry of Commerce, China
MTN	Multilateral Trade Negotiations
NAMA	Non-Agriculture Market Access
NGOs	Non-Governmental Organizations
OECD	Organization for Economic and Cooperation Development
OTDS	Overall Trade-distorting Domestic Support
SSM	Special Safeguard Mechanism
UR	Uruguay Round
US	United States of America
USDA	United States Department of Agriculture
WTO	World Trade Organization

## Chapter One: Introduction

The worldwide economic depression and the Democratic election victories in the 1930s opened a new page for the agriculture economy of the United States (US). The Agricultural Adjustment Act of 1938 arising from its 1933 version, together with the Agricultural Act of 1949, constitutes the permanent legal framework governing US agricultural policy. Every five years since then, Congress has undertaken an overhaul of the federal agriculture and food programs, which is also normally known as the Farm Bill. The farm bill is a massive piece of federal legislation covering various topics related to agriculture, including commodity price support, farm credit, food aid, tax, international trade, crop insurance, rural development and research. However, it needs to be pointed out that the farm bill is not the only federal legislation related to the US agriculture policy. There are many other pieces of legislation concerning the environment and tax and land issues which are not contained in the farm bill.

The farm bill not only affects every American citizen in one way or the other, but also attracts interest and concerns from the rest of the world. This bill influences producers and consumers both home and abroad through commodity programs, and exerts an important role in shaping the rural economy, thus directly affecting local and national agribusinesses, rural financial institutions and international agricultural trade. Actually, almost all the debates both home and abroad point to the subsidies provided through various types of commodity programs under Title I of the omnibus legislation. World-wide critics from academia, government and non-government bodies have been claiming that US subsidies through commodity programs significantly depress world market prices, lead to overproduction and adversely affect the ability of developing countries to participate in global competition.

The US has bound itself with commitments on agricultural domestic support in the World Trade Organization (WTO). Moreover, the US farm policy has always been closely related to, and even interacted with the multilateral trade negotiations. Thompson (2005) argues that “the US farm bill and multilateral trade talks, whether on parallel tracks or on a collision course, will have significant impacts on one another.”<sup>1</sup> The passage of the 2002 Farm Bill

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<sup>1</sup> Thompson, Robert. L (2005), ‘The US Farm Bill and the Doha Negotiations: On parallel Tracks or a Collision Course?’ *An IPC Issue Brief*. [www.wto.org/english/forums\\_e/ngo\\_e/posp52\\_ifatpc\\_e.pdf](http://www.wto.org/english/forums_e/ngo_e/posp52_ifatpc_e.pdf). [Accessed June 1, 2008]

was met with huge domestic policy criticism and a barrage of international condemnation. In 2002, it was even at the centre of the case brought to the WTO by Brazil against US upland cotton subsidies because Brazil declared that the US cotton subsidies had a harmful effect on world prices. The Appellate Body in 2005 ruled that the US cotton subsidies constitute significant price suppression within Article 6.3 (c) of the Agreement on Subsidies and Counter-veiling Measures (ASCM) and fail to comply with Annex 2 of the Agreement on Agriculture(AoA)<sup>2</sup>, and it further ruled in 2008 that the US does not conform to the previous DSB rulings<sup>3</sup>.

As has been clearly written in the Doha Declaration, one of the major objectives in the Doha Work Program is to substantially reduce the overall trade-distorting domestic support (OTDS)<sup>4</sup>, particularly those provided by the developed countries led by the European Union (EU), US and Japan. The rest of the world, even the US Administration requested that Congress take the lead and draft a less trade-distorting legislation with a view to reforming its agricultural policy and push forward the multilateral negotiations. The Administration on 10 January 2007 released a farm bill proposal, alleging that this proposal would lead to the incremental reforms that were “equitable, predictable and beyond challenge”<sup>5</sup>. Meanwhile, Brazil and Canada successively on January 8, 2007 and July 17, 2007, initiated separate but similar WTO cases against certain US farm programs as they relate to the US present commitments in the WTO, with a view to pressing the US to reduce its trade-distorting agricultural subsidies. In addition, the soaring world commodity prices last year also offered an opportunity for the US to undertake the agriculture reform and bind its subsidies at a lower level.

In late 2007, the House of Representatives and the Senate successively passed their own version of the 2007 Farm Bill. From February 2008 to early May 2008, the Conferee committee established by the Congress took charge and worked out a combined farm bill. The new conferee agreement caused strong opposition from the Administration, non-governmental organizations and academia due to its failure to reform the subsidy system. In spite of this, the Congress still approved it. After the Administration vetoed the bill, both the Senate and the

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<sup>2</sup> WTO (2008), US-Subsidies on Upland Cotton, *WTO Dispute Settlement One Page Case Summaries 1995-2007*. p.99. [http://www.wto.org/english/res\\_e/booksp\\_e/dispu\\_summary08\\_e.pdf](http://www.wto.org/english/res_e/booksp_e/dispu_summary08_e.pdf), [Accessed July 20, 2008].

<sup>3</sup> WTO(2008), DSB adopts compliance reports in US cotton case, *World Trade Organization 2008 News Items*, [http://www.wto.org/english/news\\_e/news08\\_e/dsb\\_20june08\\_e.htm](http://www.wto.org/english/news_e/news08_e/dsb_20june08_e.htm). [Accessed July 20, 2008].

<sup>4</sup> WTO (2001), Doha Declarations, 20 November 2001. published by the WTO Secretariat. p.6

<sup>5</sup> Johans, Mike (2006), *Remarks to the 2006 Agricultural Outlook Forum Farm Policy: A Portfolio of Economic Opportunity for Rural America*. February 16, 2006. <http://ageconsearch.umn.edu/bitstream/333167/do06jo51.pdf>. [Accessed June 20, 2008].

House of Representatives overrode the veto and made it law. Under the 2008 Farm Bill, the US farmers are likely to receive a continued stream of subsidies through the year 2012 regardless of the record farm income last year due to the strong commodity market. This legislation has attracted huge criticism at WTO talks. The negotiation groups formed by the developing countries, as well as the Cairns group and the EU, expressed their concerns with the 2008 Farm Bill, saying that the new farm bill heads agriculture policies in the wrong direction at a decisive juncture of the WTO Doha Round. Even the chairperson for agriculture negotiation, Ambassador Falconer from New Zealand, said that although the new bill did not directly affect WTO negotiations, it would have a negative effect<sup>6</sup>.

The mini-ministerial conference held in Geneva in July 2008 was regarded as a decisive step towards conclusion of the Doha Round by the end of 2008. The US chief WTO negotiator Susan Schwab offered to reduce the Overall Trade-distorting Domestic Support (OTDS) level to \$14.5 billion. However, this proposal was refused by other Members. The official US position states that the new proposal will substantially reduce the OTDS that the US can enjoy but the developing countries require the US to do more. Although the 2008 Farm Bill is not the direct factor causing this collapse, the failure of the July effort in some way has close connections with the Bill.

This short paper attempts to examine the relationship between commodity support in the 2008 Farm Bill and the on-going Doha negotiations. Have the 2008 Farm Bill undertaken subsidy reform as requested by the developing countries and the US Administration? Will the 2008 Farm Bill impose serious problem for the US before the WTO? Will the US accept the Chairperson Ambassador Falconer's latest paper on agriculture negotiations? Will the 2008 Farm Bill be the stumbling block or the building block to the conclusion of this Doha round? Chapter two illustrates the changes in trade impact under the new 2008 Farm Bill and assesses its impact on U.S farmers, tax payers and on government expenditure. Chapter three reviews the commodity programs under the current WTO rules. Chapter four analyzes commodity subsidies in the context of Ambassador Falconer's latest paper. Chapter five is the conclusion.

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<sup>6</sup> Reuters (2008), 'Farm Bill Attracts criticism at WTO talks'. *Reuters*. 26 May, 2008. <http://www.reuters.com/article/topNews/idUSL2611868820080526> [Accessed May 27, 2008].

## Chapter Two: Program Support under the 2008 Farm Bill

*“The 2008 farm bill generally continues the farm commodity price and income support framework of the 2002 farm bill, with modifications.”*<sup>7</sup> (Jim Monke)

### 2.1 General features

The Food, Conservation, and Energy Act of 2008 (also known as the 2008 Farm Bill) is the five-year omnibus legislation governing the US agricultural policy during 2008-2012. It provides agricultural subsidies to domestic producers, regulates the domestic poverty and nutrition program, supports agricultural research and investment, international and national food aid and agricultural trade. The basic structure of the 2008 Farm Bill remains the same as that of the previous ones; it is divided into titles according to their respective coverage. According to the US Congressional Budget Office (CBO), if the 2008 Farm Bill comes into effect, spending on the programs it covers would total about \$307 billion. Of that sum, \$209 billion is for nutrition programs, \$35 billion is for agricultural commodity programs, \$25 billion is for conservation programs, and the remaining \$38 billion is for other smaller programs<sup>8</sup>. Meanwhile, the Institute for Agriculture and Trade Policy (IATP) offered another cost breakdown of the bill, which is slightly different from the CBO prediction<sup>9</sup>: food stamps and other domestic nutrition programs cost about \$200 billion, which is over 66 percent of the whole expenditure; commodity programs subsidies for rice, cotton, corn, soybean, wheat and other crops take \$43 billion, covering 14 percent; conservation programs takes 9 percent about \$27 billion, while expenditures for international food aid will be less than \$200 million.

With regard to the commodity programs, commodity support provisions in the US farm bill generally include three primary types of program: (1) the annual-paid direct payments which the US government claims to be unrelated to historical production or prices; (2) the

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<sup>7</sup> Monke, Jim (2008), *Farm Commodity Programs in the 2008 Farm Bill. CRS Report for Congress*. Order Code RL34594. p.1.

<sup>8</sup> CBO (2008), *Farm Bill Cost Estimate*. Congressional Budget Office letter to the Congress. May 13, 2008. <http://www.cbo.gov/ftpdocs/92xx/doc9230/hr2419conf.pdf>. [Accessed May 20, 2008].

<sup>9</sup> IATP (2008), *Glance: A cost breakdown of farm bill programs*. IATP Farm Bill Briefs. May 14, 2008. <http://www.agobservatory.org/headlines.cfm?refID=102704>, [Accessed May 20, 2008].

counter-cyclical payments (CCPs) to be triggered automatically when effective prices are below the target price; (3) the marketing assistance loans (MALs) providing interim finance and additional income support.

In addition, to keep the fundamental features of these commodity programs, the 2008 Farm Bill also creates a pilot revenue-based counter-cyclical program and a planting flexibility pilot program.

## **2.2 Changes with a trade impact**

### **2.2.1 Eligibility of recipients**

Whether a farmer can receive program payment depends on the eligibility criteria. The average adjusted gross income (AAGI) means the average of the portion of adjusted gross income of the person or legal entity that is attributable to activities related to agriculture. The 2002 Farm Bill requires that a person or entity with average adjusted gross income exceeding \$2,500,000 shall not be eligible to receive any subsidies, unless at least 75 percent of the income is derived from agriculture. In other words, the producer is not eligible to receive subsidies, if his/her AAGI from non-farm activities exceeds \$625,000.

The 2008 Farm Bill has more detailed provision on the eligibility of producers. If the non-farm AAGI exceeds \$500,000, the person or entity is not eligible to receive any benefits from direct payment, counter-cyclical payment, marketing loan gain or loan deficiency payment and milk income loss contract programs. Meanwhile, if the AAGI of the person or legal entity exceeds \$750,000, the person/legal entity is not eligible to receive direct payment. However, there is no such eligibility limit on the marketing assistance loans.

Minimum farm size is another factor affecting the eligibility of payment. According to the 2008 Farm Bill, if the sum of base acres on a certain farm is 10 acres or less, the producer on that farm is not eligible to receive direct payment, counter-cyclical payments or average crop revenue election payment.

### **2.2.2 Change of subsidy rate and subsidy coverage**

The 2008 Farm Bill continues the major support programs found in the previous farm bills, including the direct payment, CCPs and MALs during 2008-2012. Meanwhile, the new

bill made some adjustment on base acreage, target prices and loan rates for some commodities.

‘Direct payment’ is the payment provided to certain commodity producers based on the historical production acres and yield, which was introduced in the 2002 Farm Bill as the successor to the Plant Flexibility Contract Program in the 1996 Farm Bill. As was the case under the production flexibility contract program, producers were not required to grow any particular crop in order to receive direct payments, and could choose to grow nothing at all. In the 2008 Farm Bill, the eligible crops to receive direct payment include wheat, corn, grain sorghum, barley, oats, upland cotton, rice, soybean, other oilseeds and peanut. The formula of direct payment is as below:

$$\text{Amount of Payment} = (\text{payment rate}) * (\text{payment acres}) * (\text{payment yield})$$

Payment acres are certain percent of the base acres of a covered commodity on a farm, and the payment yield is the yield established for that commodity on that farm. Compared to the 2002 Farm bill, there is a slight change in the new bill. The payment rates used to make direct payment and eligible crops in the 2008 Farm Bill remain the same as those in the 2002 Farm Bill. However, the payment acres in the case of direct payment are reduced from 85 percent of the base acres to 83.3 percent from 2009 through 2011 crop years. In addition, producers can elect to receive advance payments of up to 22 percent of direct payment beginning December 1 of a calendar year before the year covered commodity is harvested, a limit which was reduced from 50 percent in the 2002 Farm Bill.

With regard to the planting flexibility, fruits and vegetables (other than lentils, mung beans, and dry peas) and wild rice are still on the list of planting flexibility limitations. However, the bill establishes a planting transferability pilot program to permit the planting of fruits and vegetables on the base acres of 75,000 acres in seven Midwestern states. In order to be eligible for the pilot, producers had to have entered into contract to produce the specified crop for processing, agree to produce crop as part of a program of crop rotation, and provide evidence of disposition of crop.

‘Counter-Cyclical Payments’ (CCPs) are subsidies provided to certain crop producers based on historical production and yield. The payment amounts equal the CCP rate times the farm’s payment acres times the farm’s CCP yield. When the effective price for the covered commodities is less than the target price already set up, the covered producers can receive

CCPs. The effective price is the direct payment rate plus the higher of national average market price in the 12-month marketing year and national average loan rate for a marketing assistance loan.

With regard to the CCPs, the 2008 Farm Bill increases the target prices for most crops covered in the 2002 Farm bill, with only upland cotton price slightly reduced, as can be seen in Table1. Additionally, four more commodities, including dry peas, lentils, small chickpeas and large chickpeas are added as eligible for the CCP. The new bill also has changes on the percentage of partial payment, and the partial payments are not available until the 2011 crop year.

Table 1: Target Prices for Counter Cyclical Payments under 2008 Farm Bill

Commodities	2002 Farm Bill	2008 Farm Bill		Changes
	2004-2007	2008-2009	2010-2012	
Wheat	\$3.86/bu	\$3.92/bu	\$4.17/bu	↑
Corn	\$2.60/bu	\$2.63/bu	\$2.63/bu	↑
Sorghum	\$2.54/bu	\$2.57/bu	\$2.63/bu	↑
Barley	\$2.21/bu	\$2.24/bu	\$2.63/bu	↑
Oats	\$1.40/bu	\$1.44/bu	\$1.79/bu	↑
Cotton	\$0.7240/lb	\$0.7125/lb	\$0.7125/lb	↓
Rice	\$10.50/cwt	\$10.50/cwt	\$10.50/cwt	-
Soybean	\$5.80/bu	\$5.80/bu	\$6.00/bu	↑
Other Oilseeds	\$0.1010/lb	\$10.10/cwt	\$12.68/cwt	↑
Dry peas	-	\$8.32/cwt *	\$8.32/cwt	↑
Lentils	-	\$12.81/cwt *	\$12.81/cwt	↑
Small chickpeas	-	\$10.36/cwt *	\$10.36/cwt	↑
Large chickpeas	-	\$12.81/cwt *	\$12.81/cwt	↑

Source: the 2008 Farm Bill.

\*payment applicable from the year 2009

‘Marketing Assistance Loans’ (MALs) are non-recourse loans that farmers can receive by pledging their commodity as collateral. It provides the producers with interim financing at harvest or shearing time to meet cash flow needs without having to sell their commodities

when market prices are typically at harvest-time lows. During the implementation period of the 2008 Farm Bill, the loan rate in the year 2008 applies to those as defined in the 2002 Farm Bill for the year 2007. All the possible changes on loan rate will come into force at least from the year 2009. Among the eligible crops for the MALs, the loan rates for most crops either remain at the same level as those in the 2002 Farm bill, or increase at a rate varying from four percent to thirteen percent. For the commodities including corn, grain sorghum, upland cotton, extra long staple cotton, rice, and soybeans, there are no loan changes during the whole farm bill implementation. For dry peas and lentils, the loan rates are slightly reduced in the year 2009 and will remain that level thereafter. It is also remarkable that a new loan rate is created for the large chickpea in the new legislation from 2009.

Besides that, if the eligible producers obtaining a loan agree to forgo the loan, they may receive the loan deficiency payment (LDPs). The LDP equals the LDP rate times the quantity of the commodity for which the LDP is requested. The LDP rate equals the amount by which the applicable loan rate where the commodity is stored exceeds the alternative loan repayment rate for the respective commodity. There is no change between 2008 Farm Bill and 2002 Farm Bill in this regard.

Table 2: Changes of National Loan Prices for MALs

Commodities	2002 Farm Bill	2008 Farm Bill			Change
	2004-2007	2008	2009	2010-2012	
Wheat	\$2.75/bu	\$2.75/bu	\$2.75/bu	\$2.94/bu	↑
Corn	\$1.95/bu	\$1.95/bu	\$1.95/bu	\$1.95/bu	-
Sorghum	\$1.95/bu	\$1.95/bu	\$1.95/bu	\$1.95/bu	-
Barley	\$1.85/bu	\$1.85/bu	\$1.85/bu	\$1.95/bu	↑
Oats	\$1.33/bu	\$1.33/bu	\$1.33/bu	\$1.39/bu	↑
Soybeans	\$5.00/bu	\$5.00/bu	\$5.00/bu	\$5.00/bu	-
Other Oilseeds	\$9.30/cwt	\$9.30/cwt	\$9.30/cwt	\$10.09/cwt	↑
Rice	\$6.50/cwt	\$6.50/cwt	\$6.50/cwt	\$6.50/cwt	↑
Cotton	\$0.52/lb	\$0.52/lb	\$0.52/lb	\$0.52/lb	-
Peanuts	\$355.00/t	\$355.00/t	\$355.00/t	\$355.00/t	-
Honey	\$0.60/lb	\$0.60/lb	\$0.60/lb	\$0.69/lb	↑
Wool, graded	\$1.00/lb	\$1.00/lb	\$1.00/lb	\$1.15/lb	↑
Mohair	\$4.20/lb	\$4.20/lb	\$4.20/lb	\$4.20/lb	-
Dry peas	\$6.22/cwt	\$6.22/cwt	\$5.40/cwt	\$5.40/cwt	↓
Lentils	\$11.72/cwt	\$11.72/cwt	\$11.28/cwt	\$11.28/cwt	↓

S. chickpeas	\$7.43/cwt	\$7.43/cwt	\$7.43/cwt	\$7.43/cwt	-
L. chickpeas	-	-	\$11.28/cwt	\$11.28/cwt	↑

Source: 2008 Farm Bill and 2002 Farm Bill.

### 2.2.3 Creation of the ACRE Program

The 2008 Farm Bill creates a new subsidy program to provide a safety income net for the farmers. From the beginning of 2009, farm producers are given the option of staying with the current program or switching to a new support program called Average Crop Revenue Election Program (ACRE).

For the traditional programs, the amount of money that farmers can receive depends on the level of commodity prices. The concerned farmers will automatically receive payment when the prices are low enough. The big change is that the ACRE program is paid under the following conditions: first, the actual state revenue for the given crop in the given crop year falls below the specified trigger level called the ACRE program guarantee; second, actual farm revenue for the given crop in the given crop year is less than the farm ACRE benchmark revenue. The actual state revenue is based upon actual state yield and national average market price in the crop year.

The ACRE program guarantees equals to 90 percent of the sum of benchmark state yield and the ACRE program guarantee price. The benchmark state yield is based upon the five-year average yield per planted acre (excluding the highest and the lowest yields), while the guarantee price is the simple average of the national average market price in the recent two years.

The amount of ACRE program is the sum of state average revenue payment rate, payment acreage and quotient. The state average revenue payment rate is the difference between the ACRE program guarantee and actual state revenue, which shall not exceed 25 percent of the program guarantee. The ACRE payment acreage is 83.3 percent of the acreage planted from 2009 to 2011 and 85 percent in the year 2012. The quotient is obtained by dividing the five-year average yield per planted acre by the benchmark state yield.

However, there are several points which need to be emphasized: First, the eligible crops to ACRE subsidies are only the commodities covered by direct payments and counter-cyclical payment plus peanut. In other words, like the CCPs, not all the commodities can receive the

subsidies. If the farmers decide to pick the ACRE, they have to register all their eligible crops to this program. Second, in order to receive ACRE, the farmers have to reduce their direct payment and market assistance loan by 20 percent and 30 percent respectively. For the farmers, if the commodity prices continue to go up, ACRE will not be triggered and the farmers have to bear 20 percent reduction of the direct payment; in the contrary, if crop prices substantially reduce, ACRE payments are likely to be larger. In other words, the objective of ACRE program is to diminish the decline of revenues, whether the price is high or low. Moreover, farmers choosing to join the ACRE program must stay in the program through 2012. Third, the change of ACRE program guarantee is not allowed to exceed or decrease more than 10 percent from the previous year.

#### 2.2.4 Payment Limitation

Producers may receive different types of program payments; however, each type of payments has its limitation, which has been effective since the Agriculture Act of 1970.

The 2008 Farm Bill does not modify the payment limit granted to the direct payment and counter-cyclical payment, as is defined \$40,000 and \$65,000 under the 2008 Farm Bill respectively. With regard to the newly-established ACRE, the new bill has more detailed provision. If the producers also choose ACRE, the annual payment limit is \$40,000 less the amount of reduction in direct payment. For those producers who choose ACRE and CCPs, the payment limit shall not exceed the sum of CCPs and the amount of direct payment reduced due to the participation of this program. It should be pointed out that while a \$75,000-per-person payment limitation for each crop year is set up in the 2002 Farm Bill, there is no similar language in the 2008 Farm Bill. In other words, there is no payment limitation for the marketing assistance loans, which is strongly criticized by many developing countries.

#### 2.2.5 Dairy and Sugar Program

For the sugar program, the new bill increases the loan rates for sugarcane and sugar beets. The loan rates for the processors of domestically grown sugarcane are increased by 0.25 cent per pound every year from 2009-2011, while the final loan rate in 2012 remains the highest at 18.75 cent per pound. For the processors of domestically grown sugar beets, they can receive 128.5 percent of the sugarcane loan rate beginning from 2009. The new bill also sets an al-

lotment quota to a minimum of 85% of domestic sugar consumption, meaning that no more than 15% of US consumption can come from imported sugar. If imported sugar exceeds that level, the government will buy the surplus and sell it to ethanol producers.

However, the changes to the dairy program are still more complex. With regard to the milk price support program, the 2002 Farm Bill provides that the purchase price shall be no less than the rate of price support for milk (\$9.90/cwt for milk containing 3.67 percent butterfat), while the 2008 Farm Bill sets different prices: minimum cheddar cheese prices at \$1.1-1.3 per pound, butter \$1.05 per pound and nonfat dry milk at \$0.80 per pound. Further to that, the new bill authorizes the Secretary of USDA to adjust the minimum purchase prices according to the inventory quantities. Second, the Milk Income Loss Contract program (MILC) goes through 2012, which compensates dairy producers when monthly milk price falls below a target price of \$16.94/cwt. The MILC support will be paid to the producers at the rate of 45 percent of the difference between the average monthly milk price in Boston and the target price. And the payment quantity will not exceed 2,985,000 pounds during the whole implementation period.

### **2.3 Assessment**

Agriculture is an important sector in the US economy, and it covers about 9 percent of the whole export and contributes positively to the country's trade balance. Meanwhile, agriculture is heavily subsidized with government expenditure based on the omnibus legislation. The Congress legislators have consistently argued that the objective of the legislation is aimed at establishing an income safety net for the US farmers. However, the US farm bills, in particular the 2002 Farm Bill are broadly criticized as an abolition of the US leadership in agricultural reform and in multilateral negotiations, mainly because of its commodity support provisions in the form of amber box under the WTO criteria. Since then, major exporting countries from the developing world have been trying their best to press the US Congress to write a new bill to change the situation and even the Administration expected Congress to contribute to a reduction of the government budget deficit. Soaring commodity prices provided an opportunity for the 2008 Farm Bill to further enhance the role of market signals in guiding producer decisions and to better target improvements in environmental outcomes. However, from

the day that the House of Representatives passed its draft until the final passage of the Farm Bill, words like “harvest of disgrace”, “farcical” and “shameful” have appeared dozens of times in the media<sup>10</sup>. In my opinion, discussed below, although it has taken a little step toward a modest reform, the US agricultural subsidy system has remained fundamentally unchanged under the 2008 Farm Bill.

### 2.3.1 A little step toward modest reform

Most Congress legislators probably knew that passing such a farm bill at a time of soaring crop prices was hardly to be proud of; however, there are many supporters of the farm bill such as Congressmen, farmer association and producer associations, some even from the environment NGOs or farm associations, including American Farmland Trust (AFT)<sup>11</sup>. On one hand, this reflects again the overwhelming success of the farm lobby; on the other hand, this implies that their expectations and views are embodied in some provisions of the 2008 Farm Bill.

Compared to the 2002 Farm Bill, the disciplines on the eligibility of subsidy recipient have strengthened. The new bill provides that individuals with an adjusted gross income of more than \$750,000 are not eligible to receive any commodity programs, regardless of direct payment, counter-cyclical payment or marketing loans. Considering the threshold of \$2.5 million in the 2002 Farm Bill, this can be considered as progress, although this ceiling is less reform-minded compared with the proposal of \$200,000 limit suggested by the US Administration. Moreover, the new bill provides that deceased persons are not eligible to directly or indirectly receive payments, for which the previous farm bill had no such provisions at all. This provision helps to reduce the amount of subsidies granted to illegal recipients.

Additionally, the payment acres in the case of direct payment are reduced from 85 percent of the base acres to 83.3 percent from the year 2009 through 2011 crop years. The reduction of payment acres will certainly lead to the deduction of the payment amount granted to the farmers, taking the calculation method of direct payment into account.

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<sup>10</sup> See “The Farm Bill: A harvest of disgrace” in *The Economist*, May 22nd, 2008. [http://www.economist.com/world/unitedstates/displaystory.cfm?story\\_id=11412562](http://www.economist.com/world/unitedstates/displaystory.cfm?story_id=11412562) and “A few good ideas leaven farm bill, but overall it’s a shameful harvest - editorial” on *Cleveland.com*. May 27, 2008. <http://www.cleveland.com/editorials/plaindealer/index.ssf?/base/opinion/1211877085236540.xml&coll=2>

<sup>11</sup> AFT (2008), AFT and 1054 Organizations support the farm bill. AFT farm bill Brief. May 21, 2008. [http://www.farmland.org/programs/campaign/documents/5-21-08-senate\\_veto-override-coalition-ltr.pdf](http://www.farmland.org/programs/campaign/documents/5-21-08-senate_veto-override-coalition-ltr.pdf). [Accessed August 20, 2008].

### 2.3.2. Fundamentally unchanged system

Generally speaking, despite some minor reforms there was no attempt to undertake the necessary fundamental reforms. In other words, the 2008 Farm Bill does nothing to reverse trends toward increased farm concentration, indirect feed subsidies to industrial meat production and agricultural markets or rising food prices.

Congress failed to take the opportunity to make the right decision at the right time. When the 2002 Farm Bill was approved, the whole world was in a rage at the commodity provisions, expecting that legislators could undertake real reforms five years later<sup>12</sup>. However, according to the USDA statistics, the average farm household income has exceeded average US household income since 1996<sup>13</sup>. And the average household income of principal US farm operators (from farm and off-farm sources) is projected to increase again by 7.7 percent in 2007, to \$83,622, which implies that the subsidies for farmers are no longer necessary from a poverty-reduction perspective. Nevertheless, Congress ignored these facts and maintained the expensive subsidy system by allocating billions of dollars to conglomerates and special interest groups such as American Soybean Association and the US Wheat Associates.

The continuation of direct payments enables the farmers to get extra benefits from production, even though the commodity prices are already high. The exclusion of vegetables, fruits and wild rice from payments has the potential to channel production towards the production of crops that remain eligible for payments. Together with other loopholes, the net result is virtually no change in the highly-skewed *status quo* on payment limits for direct and countercyclical payments. Worse, the existing per farm limits for the loan deficiency payments were removed, so that those payments are now completely unlimited. Moreover, the coverage of the eligible commodities is expanded to more crops. Even with regard to the farm size eligibility of subsidy recipient, while this is a step in the right direction, these changes are considered by many to be quite minor. Even individuals not actively engaged in farming can continue to get payments. Also, family farm operations with a combined income of \$1.25 million can still receive the maximum amount of direct payments allowed, and there is even no

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<sup>12</sup> CATO (2002), *Cato Policy Forum: Farm Bill Follies*. CATO Institute. <http://www.freetrade.org/node/365>. [Accessed September 9, 2008]

<sup>13</sup> USDA (2007), *Agriculture Income and Financial Outlook*, Report from the Economic Research Service, USDA. December 2007. p.2.

limit at all for marketing assistance loans. Besides that, the large farm operations will continue to receive the majority of the government subsidies. According to the USDA statistics, three percent of all farms receiving government payments receive sixteen percent of all government payments, while only 7 percent of all government payments went to farm operations with less than \$10,000 in sales—a group accounting for 35 percent of all farms receiving government payments<sup>14</sup>.

Third, the new farm bill is bad for the US consumers, taxpayers and the image of the U.S in the global community. Economically, agricultural subsidies have a similar effect to tariffs, i.e. increase the cost of consumers. As the Wall Street Journal describes, “If farm prices stay high, consumers face higher grocery bills and farmers get rich. If farm prices fall, taxpayers kick in the difference and farmers still get rich<sup>15</sup>”. The farmers can always get subsidies regardless of the high or low commodity prices. The think tank for the developed countries, the Organization for Economic and Cooperation Development (OECD) has a systematic record on agricultural support. It defines the producer support estimates as the annual monetary value of gross transfers from consumers and taxpayers to agricultural producers. According to that definition, the total transfer to the US producers in 2006 was 30,860 million dollars, in other words, every US citizen has to pay \$103 per year to support their farmers<sup>16</sup>. In 2006, the consumer support estimate was 124,026 million dollars, that is to say, the burden on consumers through market price support after offsetting the consumer subsidies in that year was \$413 per capita. In other words, every consumer has to pay that extra amount of money to buy food on the market. In this way, the farm bill can be considered as a bonus for special interest groups and a fine for taxpayer and consumers. In addition, the US has been criticized in multilateral trade talks for its reluctance to reduce its OTDS to a lower level. A farm bill with fewer subsidies would have shown its willingness to contribute to development and liberalization. However, the new bill facilitates the continuation and in some ways the increase of high subsidies, sending the wrong signals to the trading partners of the US and further souring the mood at the WTO where members are already facing an uphill battle to finish the Doha negotiations.

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<sup>14</sup> USDA (2007), *ibid.* p.21.

<sup>15</sup> Wall Street Journal (2008), *Changes you can't believe in*, Review and Outlook. May 22, 2008. Page A 14. <http://online.wsj.com/article/SB121141471637712559.html>. [Accessed May 23, 2008]

<sup>16</sup> OECD (2008) *Agricultural Policies in OECD Countries: At a Glance*. Published by the OECD. p.85.

### 2.3.3 Ambiguous Effect of the ACRE

For many supporters of the 2008 Farm Bill, the creation of the new ACRE program is regarded as the most important success to reform of the agriculture sector, however, the effect of this new program needs to be seen in the future.

Considering that the traditional subsidy programs have had a stimulating effect on production and trade, the new ACRE program can be seen as a step in the right direction of the US farm policy. First, compared to direct payment and counter-cyclical payment, the ACRE program is more market-oriented and less trade-distorted because it uses a revenue target that moves with the market rather than being based on a fixed rate. And it requires producers to prove that they have suffered a loss before receiving payments, which conforms to the notion of a safety net which provides assistance only when necessary and to farmers in real need. Second, the stringent conditions for the ACRE program help reduce the expenditure problem. The ACRE program requires farmers opting for this program to stick with it until the end of the new farm legislation. Even if the farmers do not receive the payment this year because they fail to meet the trigger level, they cannot move out of the program next year. Moreover, if they join the ACRE, farmers will lose 20 percent of direct payments and 30 percent of counter-cyclical payments they previously received. If the commodity price continues to go up, the farmers will receive fewer subsidies than they got before.

However, this does not mean that there is no trade-distorting effect in the ACRE program. If the market price declines and the state revenues are low enough, the ACRE can pay out more subsidies than all the traditional programs together. According to the Washington Post, the USDA stated that the ACRE program could increase the payments by billions of dollars to the farmers if high commodity prices decline to more typical levels<sup>17</sup>. What's more, the ACRE program is not open to all crops, and the participation of the program is not known yet. The USDA assumed an improbably high participation rate of 90 percent of all corn, soybean and wheat producers, while the Congressional Budget Office, independent and official budget analysts assumed dramatically lower participation rates. If the participation rate is low, the

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<sup>17</sup> Morgan, D (2008), "*Farm Bill's Subsidy Costs May Rise, Billions More Could Be Paid Through Little-Noticed Provision*". Washington Post. May 21, 2008; Page A02. [Accessed July 20, 2008].

[http://www.washingtonpost.com/wp-dyn/content/article/2008/05/20/AR2008052001581\\_pf.html](http://www.washingtonpost.com/wp-dyn/content/article/2008/05/20/AR2008052001581_pf.html).

new program will have less effect in reducing subsidies, but less probability to exceed traditional programs.

## Chapter Three: The 2008 Farm Bill under current WTO rules

*Domestic subsidies are the most perplexing, because they involve a vast range and number of government policies, many of which are perfectly justifiable as exercises of sovereign activities within a country*<sup>18</sup>. (John. H. Jackson)

### 3.1 US Commitment on agriculture support

According to Desta (2002), the term “domestic subsidy” is rarely used in international trade parlance, because its definition is very contentious<sup>19</sup>. Therefore, when the negotiators tried to introduce that term into agriculture, they chose to use the term “domestic support” to replace “domestic subsidies”, with a view to avoiding the possible problem of definition.

A major result of the Uruguay Round was to recognize the existence of domestic support in agriculture, and to discipline such support in the Agreement on Agriculture (AoA), differently from the treatment of subsidies in the SCM Agreement. Although the Uruguay Round negotiators failed to substantially reduce agricultural domestic support measures, they at least brought them into the framework of the multilateral trading system. All domestic support measures are now categorized into three types: amber box/*de minimis*, blue box and green box, which are given the colors of traffic lights. This systemic change makes it possible to further reduce farm support in new rounds of negotiation, as can be found in Article 20 of AoA.

#### 3.1.1 Amber box and *de minimis*

As defined in Article 6 of the AoA, the amber box covers all domestic support measures considered to distort production and/or trade, including measures to support prices or subsidies directly related to production quantities. Importantly, amber box is subject to reduction commitments, and the reduction commitments are expressed in terms of a “Total Aggregate Measurement of Support” (Total AMS). According to Article 1(a) of the AoA, the AMS is de-

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<sup>18</sup> Jackson, J. H (1997), *The World Trading System: Laws and Policy in International Economic Relations*, 2nd ed, The MIT Press, 1997. p.280

<sup>19</sup> Desta, Melaku.G (2002), *the Law of International Trade in Agricultural Products: From GATT1947 to the WTO Agreement on Agriculture*. Kluwer Law International. p.384.

defined as the annual level of support, in monetary terms, provided in favor of the producers of specified agricultural products or all agricultural products in general. From the Uruguay Round till now, only 35 of the 152 Members have total AMS commitments listed in Section I of Part IV of their Schedules.

For those Members with AMS commitments, the amount of support provided by the respective governments by the end of the Uruguay Round implementation period is called the Final Bound Commitment Level, which is the year 2000 for developed countries and 2004 for the developing ones. The level set for each year of the implementation period is called Annual Bound Commitment Level. It should be borne in mind that in any year the Current Total AMS—the actual amount of support provided during that year, calculated as the sum of product-specific and non-product-specific support subject to reduction commitments, must not exceed the Total AMS commitment level bound for that year in a Member’s Schedule. The annual and final bound commitment level of the US is illustrated in the following table:

Table 3: Section I of Part IV of the US Schedule

Annual and Final Bound Commitment Level (mill. US dollars)							
Base Level	1995	1996	1997	1998	1999	2000	2001
23879.1	23083.1	22287.2	21491.2	20695.2	19899.3	19103.3	19103.3

Source: the US GATT Schedule and notification.

However, as the second part of Article 1(a) provides, not all forms of domestic support have to be calculated into AMS. Article 6:4(a) provides that domestic support, whether product-specific or not, which does not exceed certain percent of the value of production of either the specific product or of total agricultural production, as the case may be, is not required to be included in the calculation of the Current Total AMS. This level of support is termed as *de minimis*, which is 5 percent for developed country Members and 10 percent for the developing ones.

According to the US notification on domestic support, the usage of AMS and *de minimis* level is as follow:

Table 4: Current Total AMS and *de minimis* level by the US

Type of Measures	Outlays (million dollars)					
	2000	2001	2002	2003	2004	2005
Year	2000	2001	2002	2003	2004	2005
Total AMS commitment	19,103	19,103	19,103	19,103	19,103	19,103
Current Total AMS	16,803	14,413	9,637	6,950	11,629	12,938
Percentage of Final commitment	88%	75%	50%	36%	61%	68%
Non-Product-Specific <i>de minimis</i>	7,278	6,828	5,101	2,801	5,778	5,862
Value of Agricultural Production	189,520	198,503	194,572	216,478	235,688	236,001
Percentage of VoP	4%	3%	3%	1%	2%	2%
Product-Specific <i>de minimis</i>	63	215	1,590	436	6,801	118

Source: G/AG/N/USA/51, G/AG/N/USA/60. Blanford and Orden (2008).

### 3.1.2 Blue Box

If direct payments under production-limiting programs meet certain conditions, they can be exempt from reduction commitments despite their trade-distorting nature. Those “amber box measures with conditions<sup>20</sup>” are known as “blue box”, and the general condition is to reduce distortion. These criteria are listed in Article 6.5 of AoA, and they relate to the fixed acreage and yields, or to a maximum of 85 percent or less of the base level, or to the fixed number of livestock heads. As claimed by many countries, the eventual objective of the blue box is to become “green”<sup>21</sup>.

WTO Members have to specify the amount of their blue box measures in the Table DS: 3 of their domestic support notifications. The WTO Secretariat recently prepared a note on the usage of Blue Box Support (TN/AG/S/14, 28 January 2005) in absolute terms as notified by the Members during 1995 to 2003. The note shows that the European Communities and Norway are the main users of blue box, while the US only notified 7 billion US dollars in the year 1995 in the form of blue box. Because the US applied level as notified to the WTO is well below its commitments, the US did not notify support as blue box. And the recent U.S notification shows that the US still did not have the intention to notify its domestic support as blue box (See G/AG/N/USA/58-60, 9 October 2007). In my opinion, the US possibly will try to use blue box measures once the possible Doha deal is reached.

### 3.1.3 Green Box

<sup>20</sup> WTO (2002), *The Boxes*, Domestic support in agriculture. 1 October 2002. World Trade Organization website. [http://www.wto.org/english/tratop\\_e/agric\\_e/agboxes\\_e.pdf](http://www.wto.org/english/tratop_e/agric_e/agboxes_e.pdf). [Accessed June 22, 2008].

<sup>21</sup> WTO (2002), Modalities Domestic support. Agriculture Negotiation Background. [http://www.wto.org/english/tratop\\_e/agric\\_e/negs\\_bkgnd33\\_moddom\\_e.htm](http://www.wto.org/english/tratop_e/agric_e/negs_bkgnd33_moddom_e.htm). [Accessed May 22, 2008]

Green box refers to those support measures that have “no or at most minimal trade-distorting effect or effect on production<sup>22</sup>”, and hence are subject to no limits at all. Annex 2 to the AoA provides for a detailed but non-exhaustive list of practices for which governments may claim exemption from reduction. The green box measures are illustrated in several ways, including general services, public stocking for food security, direct payments to producers, decoupled income support and environment programs; they are subject to policy-specific criteria. However, in order to claim as “green”, all measures must also conform to the basic criteria and conditions mentioned in the chapeau of Annex 2. Green box measures have to be notified as Table DS: 2 in Members’ notifications on their domestic support, and usually cover the largest proportion of the domestic support.

The recent usage of green box by the US is as follow:

Table 5: Usage of Green Box by the US during 2000-2005

Measure and Type	Outlays (million dollars)						
	Year	2000	2001	2002	2003	2004	2005
General services		8,554	9,214	10,258	10,942	11,198	11,345
Public Stockholding for Food Security		0	0	0	0	0	0
Domestic food aid		32,377	33,916	38,013	42,376	45,861	50,672
Decoupled income support		5,068	4,100	5,301	6,488	5,270	6,164
Income insurance and safety-net programs		0	0	0	0	0	0
Payments for relief from natural disasters		2,141	1,421	2,121	1,694	1,964	169
Structural adjustment through producer retirement programs		0	0	0	0	0	0
Structural adjustment through resource retirement programs		1,476	1,624	0	0	0	0
Structural adjustment through investment aids		132	106	124	112	93	79
Environmental payments		309	291	2,505	2,450	3,039	3,400
Payments Under Regional Assistance Programs		0	0	0	0	0	0
Other		0	0	0	0	0	0
Grand Total		50,057	50,672	58,321	64,062	67,425	71,829

Source: G/AG/N/USA/51 and G/AG/N/USA/60.

## 3.2 Criticism from other WTO Members

### 3.2.1 Challenges under the regular session of Committee on Agriculture

According to the terms of reference decided by the General Council in 1995, the Committee on Agriculture (CoA) “shall oversee the implementation of the AoA and afford Mem-

<sup>22</sup> WTO (1995), Agreement on Agriculture. *the Results of Uruguay Round of Multilateral Trade Negotiations: the Legal Text*. China Law Press. p.48.

bers the opportunity of consulting on any matter relating to the implementation of the provisions of the Agreement<sup>23</sup>”. Based on this mandate, the CoA meets at regular intervals to review progress in the implementation of the Uruguay Round reform programme and Members may raise any matter relevant to the implementation commitments under Article 18:6 of AoA and request the relevant Member to provide in writing specific information, or an explanation of the relevant facts or circumstances.

This author has researched the frequency of issues raised in respect of the US agricultural subsidies during the regular sessions of the AoA held since 2002. The data shows that, from the 31st regular session held in 2002 till mid 2008 matters related to the US agricultural subsidies have been raised 26 times and the major challenging parties are the agricultural exporting countries including Australia, Brazil, Canada, the European Communities, New Zealand and Thailand. The matters raised by the Members not only cover the farm bill itself, but also the detailed commodity programs.

The major issues challenged are summarized in the following table:

Table6: Major Issues Challenged under Regular Session of CoA (2002-2008)

Issues that have been raised	Frequency
Skimmed Milk Powder (SMP)	8
Food Aid	5
Farm Security and Rural Investment Act of 2002	4
Domestic Support Payments to Rice	2

*Source:* the Author’s calculation.

Particularly, either due to the pressure from other Members and the chairperson of CoA or well-knit domestic preparation, the U.S finally submitted its domestic support information during 2002-2005 to the CoA on October 4, 2007 – the final large country to do so. In the following regular session of CoA, questions regarding the US notifications dominated the half-day meeting as can be found on the website of WTO<sup>24</sup>. Direct payments and counter-cyclical payments authorized in the US farm bill were the hotspot in the discussions that day, i.e., the categorization of direct payments as “green box”, and of counter-cyclical payments as “non-product-specific”. The US delegation argued that its commodity programs fully

<sup>23</sup> WTO (1995), WTO Committee on Agriculture, *Decision by the General Council on 31 January 1995*, WT/L/43, 17 February 1995.

<sup>24</sup> WTO (2007), Spotlight on US domestic support in Agriculture Committee, 21 November 2007, *WTO: 2007 News Item*. [http://www.wto.org/english/news\\_e/news07\\_e/ag\\_com\\_21nov07\\_e.htm](http://www.wto.org/english/news_e/news07_e/ag_com_21nov07_e.htm). [Accessed 21 Nov.2007]

conformed to the requirements under the AoA, but there are is no publicly available information on how this debate went.

### 3.2.2 Challenges under the Trade Policy Review

In order to enhance the transparency of Members' trade policies and facilitate the smooth functioning of the multilateral trading system, WTO Members through Annex 3 of the Marrakesh Agreement Establishing the World Trade Organization, decided to establish a surveillance mechanism, i.e. the Trade Policy Review Mechanism (TPRM) to monitor and improve adherence of members to rules, disciplines and commitments under the trading system. All WTO members are periodically reviewed under this mechanism, the frequency of each country's review varying according to its share of world trade. However, TPRM is not intended to serve as a basis for the enforcement of specific obligations under the Agreements or for dispute settlement procedures, or to impose new policy commitments on Members. As expressed in the Marrakesh Agreement, the four Members with the largest shares of world trade are subject to this examination every two years, and now the US (together with China, European Union and Japan) is on that list.

The most recent and ninth trade policy review of the US was conducted in June 2008, and the Secretariat has just released the review report of the US trade policy<sup>25</sup>. In the chapter on agriculture, the Secretariat Report appreciates the decline of overall support to agriculture while noting that the decline reflects higher commodity prices rather than policy changes. The report further points out that some commodities including sugar and milk continue to receive high levels of support and certain commodity programs provide incentives inconsistent with market signals. The report further considers the current environment of high commodity prices as a favorable juncture to introduce policy changes to further improve the market orientation of the US agriculture policy.

In the review meeting, many WTO Members and particularly agricultural exporting countries, also treasured this opportunity and put forward many questions related to agriculture subsidies during the discussions. The questions included both cross-cutting issues and detailed ones: why did the US not take the opportunity of historic favorable crop prices to

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<sup>25</sup> WTO (2008), Trade Policy Review: United States, Revision. *Report prepared by the Secretariat*. 12 August 2008. WT/TPR/S/200/Rev.1. Downloadable from the WTO Member's website.

reform its agriculture sector; will the expenditure of the 2008 Farm Bill exceed the extension of 2002 Farm Bill; how could the US anticipate meeting current commitment levels on domestic support and any future commitments under a Doha deal; how could the US justify its direct payments as “green box” measures and counter-cyclical payments as non-product-specific under the AoA, etc. With regard to the 2008 Farm Bill, the US simply replied that the Administration will implement the Farm Bill approved by the Congress in spite of the (earlier) veto from the President. With regard to the details, the US repeated the usual replies at the regular session of the CoA.

Now the Administration has begun to implement the 2008 Farm Bill, it is expected that the implementation of the new farm bill will be under hot scrutiny in the next trade policy reviews as well as in AoA.

### 3.2.3 Challenges under the Dispute Settlement Body

Dispute settlement is the central pillar of the multilateral trading system, and the WTO’s unique contribution to the stability of the global economy. A dispute arises when a country adopts a trade policy measure that another Member claims to be inconsistent with the WTO agreements or obligations of that country. Without a means of settling disputes, the rules-based system would be less effective because the rules could not be enforced. The procedure for settling trade disputes existed under the old GATT, but it had no fixed timetables, rulings were easy to block, and many cases dragged on for a long time inconclusively. In order to make the mechanism more effective, the negotiators in the Uruguay Round introduced a more structured process with clearer defined stages in the procedure and stricter disciplines for the duration of a case with deadlines set for the various stages of the procedure. If a responding party refuses to change its measures ruled inconsistent by the DSB with its WTO obligations, the DSB can authorize the complaining party to retaliate by raising its MFN tariffs for imports from the respondent.

In September 2002, Brazil filed a WTO dispute case against the US cotton program, alleging that the US subsidies or support measures benefiting cotton violated the provisions under the AoA and the ASCM<sup>26</sup>. In the end, the US lost the case on most counts at both the

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<sup>26</sup> WTO (2002), Request for Consultations by Brazil, United States-Subsidies on Upland Cotton. WT/DS267/1, October 3, 2002. Downloadable from WTO website.

Panel and the Appellate Body levels. The DSB ruled that the US domestic cotton subsidies exceeded WTO commitments of the 1992 benchmark year, that direct payments and plant flexibility contracts did not qualify for the green box defined in the AoA, and that the price-contingent subsidies were significant price suppression within the meaning of Article 6.3(c) of the ASCM.

The cotton case throws a new spotlight on the conflict between US subsidy programs and the WTO rules and may constitute a precedent for other similar cases. After Brazil's successful challenge in the US cotton case, Canada decided to bring the US farm programs again before the DSB. On 8 January 2007, Canada initiated a dispute settlement case against certain the US commodity programs in general and particularly for corn<sup>27</sup>. Canada's claims were focused on two aspects: first, Canada claimed that the domestic support provided by the US government had exceeded its annual commitment level for the AMS in each of the years 1999 to 2005; second, the US export credit guarantee programs are claimed to be a WTO-illegal export subsidy. Brazil on 11 July 2007 also requested consultations with the US under the DSU procedures to discuss two charges against US farm programs similar to Canada's claims<sup>28</sup>. Upon the request from both Canada and Brazil, the DSB established a single panel on 17 December 2007.

Brazil and Canada chose a critical time to sue the US subsidies before the DSB. After the G6 failed to reach consensus on agriculture and NAMA modalities on 23 July 2006, WTO Director General Pascal Lamy recommended the suspension of negotiations across the Round as a whole and the General Council supported that recommendation on 27 July 2006. After that, the negotiations turned to quiet diplomacy among major members. In February 2007, with voice from all sides calling to put the negotiations back on track, Lamy in his report to the General Council, proposed that the negotiation should resume fully across the board. Brazil and Canada resorted to the dispute settlement process to defend their interest for two reasons: to put pressure on the US to make concessions in the negotiations, or – failing that – to obtain at least a revision of US farm policies. Furthermore, the US Congress at that time was still under the drafting process of the 2007 Farm Bill and later 2008 Farm Bill. Brazil and

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<sup>27</sup> WTO (2007), Request for Consultations by Canada, United States – Subsidies and Other Domestic Support for Corn and Other Agricultural Products. WT/DS357/1, January 11, 2007. Downloadable from WTO website.

<sup>28</sup> WTO (2007), Request for Consultations by Brazil, United States-Domestic Support and Export Credit Guarantees for Agricultural Products. WT/DS365/1, July 17, 2007. Downloadable from WTO website.

Canada expected to draw the Congress' attention on the problems the farm subsidies were facing at the WTO, and to carry out reforms in the new farm legislation. More importantly, although the DSB ruling is on a case-by-case basis, the previous rulings still could shed some light for the future findings. And most of the Canadian and Brazilian claims are based on rulings from the US-upland cotton cases, which could more or less provide both countries with some confidence regarding the new cases.

### **3.3 Initial Reactions to 2008 Farm Bill from Politicians and Academia**

As mentioned above, the 2002 Farm Bill has been widely criticized for increasing subsidies with detrimental effects on world markets and for undermining the leadership of the US in reforming farm policy and liberalizing agricultural trade. On the other hand, what probably matters more for a Congress in re-election mode, most US farmers are quite happy with the 2002 Farm Bill, particularly those major commodity groups who have been the primary beneficiaries to the omnibus legislation. The massive increase in domestic food aid satisfied both farmers and food stamp beneficiaries. However, domestic criticism also pointed at the huge expenditure in this legislation, particularly at a time of massive federal budget deficits. The 2002 Farm Bill was extremely unpopular in much of the developing world claiming that the US subsidies put them in a disadvantaged position to compete in the international arena.

Generally speaking, pressures to limit the cost of the farm bill arise from two sources: tightening budget constraints and the US commitments on agriculture in the WTO. However, these two reasons proved to be as ineffective as they did for the 2002 Farm Bill.

The timetable of the major events for the 2008 Farm Bill is as follows:

Table 7: Major Events of the 2008 Farm Bill

Date	Event
Jan.31, 2007	USDA released the 2007 Farm Bill Administration proposals
Jul.27, 2007	House of Representatives passed the 2007 Farm Bill (H.R. 2419)
Dec. 14,2007	Senate passed the 2007 Farm Bill(S.2302)
Feb. 5,2008	The House and Senate establish the Conferee Committee
May 8, 2008	The Congress passed the 2008 Farm Bill Conference Agreement

May 20, 2008	The Congress sent the 2008 Farm Bill to the President
May 21, 2008	The President vetoed the Farm Bill
May 22, 2008	The Congress overrode the President Bush's veto
Jun. 18, 2008	The President vetoed the Farm Bill again
Jun. 18, 2008	The Congress overrode the President's second veto

*Source:* the Author's observation.

The drafting process of the 2008 Farm Bill has been watched carefully by the US trade partners and world-wide academia.

After the Administration released the 2007 Farm Bill proposals, the rest of world promptly issued their initial reactions. The European Commission asserted that the Administration's proposal had some modest shift toward market-oriented reform but needed further steps. Oxfam America deemed the Administration proposal as an encouraging step toward meaningful farm program reform. When the House of Representatives passed its version of the 2007 Farm Bill, the trading partners of the US warned that this was an obstacle to a successful outcome of the Doha talks. Australia's Trade Minister Truss said that the US Congress sent the wrong sort of signals to the rest of the world about the US willingness to make concessions. One senior Indian official warned that the US Farm Bill 2007 would erode the position of the US in the Doha Round negotiations, because the legislation did not provide any prospect for reducing its agricultural subsidies. When the Congress overrode the President's veto, the negotiators in Geneva again expressed their concerns. Australian Trade Minister Crean stated that the Farm Bill is shortsighted, reactive and a lost opportunity<sup>29</sup>. The agriculture negotiation group "G20" formed by developing countries, together with the Cairns Group led by Australia issued their statements respectively, criticizing that the Congress undermined all sides' efforts in the Doha Round, and called on the US to take leadership in the multilateral process of agriculture reform.

During the whole drafting process, the Administration threatened several times to veto the bill if the bill failed to be fiscally responsible and better targeted at support programs. However, the voices from the White House and relevant government agencies were not heard

<sup>29</sup> Crean, Simon (2008), New United States Farm Bill: A Lost Opportunity, 16 May, 2008. Australia Trade Minister's website. [http://www.trademinister.gov.au/releases/2008/sc\\_035.html](http://www.trademinister.gov.au/releases/2008/sc_035.html). [Accessed May 22, 2008].

by the Congress at all. When the Congress delivered their final package on the table of the White House, George W. Bush vetoed this bill as he promised, alleging that the bill is inconsistent with US objectives in international trade negotiations and in violation of a US commitment to move towards toward more market-oriented policies.

Independent research institutes and think tanks have also voiced their opposition to the farm bill. Riedl from Heritage Foundation listed seven reasons to veto the farm bill and suggested the President and reform-minded lawmakers flat-out reject the 2008 Farm Bill<sup>30</sup>. When the President vetoed the bill, Oxfam America reacted and called the Congress to follow the Administration's decision and rewrite the farm bill through cutting payments to rich farmers, reforming trade-distorting subsidies and abolishing the inefficiencies of the food aid programs<sup>31</sup>. It later reported that the 2008 Farm Bill not only contradicts existing US obligations at the WTO but also squanders the opportunity to reach a pro-development trade deal<sup>32</sup>. The Institute for Agriculture and Trade Policy, Cato Institute, the Environmental Working Group, the Center for Rural Affairs, Citizens against Government Waste, and the Episcopal Church also fault the farm bill for missing the opportunity to fix the broken subsidy and food aid system.

Generally speaking, the main flaws that politicians and academia have found in the 2008 Farm Bill focus on the following points: faced with the mounting food crisis both home and abroad, the farm bill fails to undertake the much-needed farm program reform, raises subsidy payment rates for most programs, extends the coverage of the eligible crops with commodity prices soaring, continues to subsidize the millionaires and undermines the US trade relations with other countries. Despite sky-high crop prices, the new bill raises subsidy rates for more than a dozen crops under the countercyclical and/or marketing loan programs. Raising those target prices means that any drop in crop prices would trigger the payment of subsidies sooner and cost taxpayers far more than under current law. The bill also adds four new crops to the countercyclical program. In addition, the new bill eliminates key payment limits for the marketing loan program.

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<sup>30</sup> Ridel, B.M (2008), Seven Reasons to Veto the Farm Bill, the Heritage Foundation Backgrounder, No. 2134. [http://www.heritage.org/Research/Agriculture/upload/bg\\_2134.pdf](http://www.heritage.org/Research/Agriculture/upload/bg_2134.pdf). [Accessed May 18,2008]

<sup>31</sup> Oxfam (2008), Oxfam's Reaction to Bush Farm Bill Veto, Oxfam News Release. Oxfam website. 21 May 2008. [http://www.oxfamamerica.org/newsandpublications/press\\_releases/oxfams-reaction-to-bush-farm-bill-veto](http://www.oxfamamerica.org/newsandpublications/press_releases/oxfams-reaction-to-bush-farm-bill-veto). [Accessed July 22, 2008]

<sup>32</sup> Oxfam (2008), Square pegs in round holes: How the Farm Bill squanders chances for a pro-development trade deal. Oxfam Briefing Note. July 21, 2008. <http://www.oxfam.org/files/us-farm-bill-square-pegs-in-round-holes-0807.pdf>. [Accessed July 22, 2008]

### **3.4 Personal Appreciation of the commodity programs under 2008 Farm Bill**

According to Article 18 of the AoA, different domestic support measures need to be notified regularly to ensure the transparency of the multilateral system. However, the issue of US domestic support has been contentious in the WTO and even caused several dispute cases. The question is whether the US has correctly notified its domestic agricultural support measures and whether the applied subsidies violated its commitments to the WTO. Now the 2008 Farm Bill has come into force, the question is how the US should notify its commodity programs.

The criteria for decoupled income support are defined in Annex 2 paragraph 6 of the AoA. Since the notification obligation was established, the US has consistently notified the plant flexibility contract program in the 1996 Farm Bill and the direct payment in the 2002 Farm Bill as decoupled income support.

However, the US classification of direct payments is subject to trade dispute. In the *US-Upland Cotton* case the US argued that the payments are made based on historical acreage and yields for wheat, corn, grain sorghum, barley, oats, rice, upland cotton, soybeans, other oilseeds, and peanuts. Nevertheless, the US admitted that direct payment provisions under the 1996 Farm Bill or 2002 Farm Bill may be reduced or eliminated for certain crops (planting fruits, vegetables and wild rice). The Appellate Body ruled that production flexibility contract payments and direct payments are inconsistent with the parameters for the decoupled income support, because the payment conditioning requires the producers to grow or have previously grown specified commodities and denies payments to farmers growing fruits and vegetable and/or wild rice. Therefore, these two payments under the farm bill do not qualify under Annex 2 but have to be notified as Amber box measures. If it had notified plant flexibility contract programs as an amber box measure, the total AMS level in 1999 and 2000 would have reached 22.3 and 21.8 billion dollars, violating its total AMS commitment in the respective years as can be found in Table 3. Blanford and Orden (2008) further predicted that the US would also violate its commitment in the year 2001, if the plant flexibility program had been notified as Amber box.

Now the 2008 Farm Bill maintained the direct payments to certain commodities, and

fruits, vegetables and wild rice are still out of the scope. In other words, these direct payments remain in the Amber box, and the US has to respect its commitment not to overshoot \$19.01 bn. In the 50th regular session of the AoA committee held in November 2007 in Geneva, the US representative argued against the AB ruling in Upland cotton, arguing that direct payments meet the conditions for decoupled income support.

On the assumption that the direct payments under the 2008 Farm Bill will again qualify as Amber box measures, the author calculated on the basis of the available US notifications, that average outlay for plant flexibility contract during 1996-2002 is 5.1 billion dollars, while average outlay for direct payment during 2002-2005 is 4.3 billion dollars. Meanwhile, the Environment Working Group estimates that the amount of direct payment that farmers receive in 2007 is 5.07 billion dollars<sup>33</sup>. Although the price-boosting effect of the commodity prices will help the US withstand some pressure to reduce subsidies, from the other countries, the direct payments are made automatically to qualified farm beneficiaries. It is estimated that the direct payments would be paid in the similar amount during 2008-2012, taking the unchanged payment rate and slightly change of payment acreage into account. No matter whether the direct payment is notified as product-specific AMS or non-product specific AMS, this would significantly affect total AMS level. However, it also needs to be pointed out that the US will still not violate its WTO commitments as long as the commodity prices remain high.

With regard to the CCPs, the problems are whether the U.S will notify it as non-product specific AMS, product-specific AMS, or blue box measures and whether it exceeds the US limits. The Appellate Body in US-Upland Cotton case ruled that the characteristics of CCPs demonstrates a link between payments made with respect to historic base acres and the continued production, and are paid to specific crops<sup>34</sup>.

The average amount of counter-cyclical payments specified in US notification during 2002-2005 is 2.8 billion dollars. According to Blanford and Orden (2008), if counter-cyclical payments and direct payment are categorized as product-specific support, the US would have exceeded its commitments in the year 2004 and 2005<sup>35</sup>.

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<sup>33</sup> EWG (2008), "Amidst Record 2007 Crop Prices and Farm Income Washington Delivers \$5 Billion in Subsidies". EWG website. [http://farm.ewg.org/farm/dp\\_analysis.php](http://farm.ewg.org/farm/dp_analysis.php). [Accessed May 22, 2008].

<sup>34</sup> WTO (2005), the Appellate Body Report, United States-Subsidies on Upland Cotton. WT/DS267/ABR, March 3, 2005. Downloadable from WTO website. p.291.

<sup>35</sup> Blanford, David and Orden, David (2008), 'Shadow Domestic Farm Support Notification for the United States'. *Improving WTO Transparency: Shadow Domestic Support Notification*. Washington DC. March 14-15, 2008. p.27.

The fundamental structure of CCP payments does not change in the 2008 Farm Bill. Moreover, the U.S on the November 2007 CoA meeting replied that the recipients include producers of fruit and vegetables and cannot be ascribed to a specific product. Another option before the US is to notify the counter-cyclical payments as blue box under Article 6 of the AoA, because the U.S has never notified its usage. And this has also been proposed by Murphy and Suppan (2008). However, the ruling of the Appellate Body in US-Upland Cotton implies that the counter-cyclical payments demonstrate a link between payments made with respect to historic upland cotton base acres and the continued production of upland cotton, thus, is not consistent with the criteria of blue box. Therefore, the correct notification of the counter-cyclical payments would be as product-specific and under the AMS. However, depending on actual expenditures this could bring the US expenditures beyond its current AMS commitment.

Regarding the newly created ACRE program, the US would have no choice but to classify it as product-specific amber box measures. First, the ACRE program is limited to certain commodities, which means it fails to comply with the criteria of green box. Second, the ACRE program is not based on fixed and unchanging base and yields, because only the program guarantee has the historical base and payment yield and the actual state revenue is variable.

As for the dairy and sugar programs, they will possibly be notified as the product-specific support measures, because this is how the US has consistently classified them in recent years.

Last but not least, Section 1601 of the 2008 Farm Bill provides that the Secretary of Agriculture has the final and conclusive authority to implement the funds under the commodity provision of the bill, which is really worth emphasizing. Many developing countries are quite aware that they can bring the US farm subsidy program before the WTO; however, this will not necessarily occur due to the existence of this provision. This provision allows the Secretary to have the discretion to decide the payment acreages, payment yield and annual outlay level and authorizes the Secretary to take adjustment measures to comply with the trade agreements that the US has signed. That is to say, even though the theoretical budget outlay of the 2008 Farm Bill exceeds the possible US commitment after the Doha Round, the Secretary can choose to reduce the spending amount in order to comply with the Doha com-

mitment.

## Chapter Four: The 2008 Farm Bill in the Post-Doha Era

*I was quite transparent in saying that this farm bill is not sending a great signal that the US is serious about reducing their trade-distorting subsidies. The only chance you have to trump up this farm bill is the WTO deal which will then necessitate a reform of the US system*<sup>36</sup>. (Pascal Lamy)

### 4.1 Development of Negotiations

One of the big successes in the Uruguay Round negotiations as broadly considered is that the WTO Membership for the first time agreed to establish a set of principles and disciplines to discipline and reduce trade distortions resulting from agricultural policies such as the ones used during the past decades. But this was only the first phase. Article 20 of the AoA committed members to start negotiations on continuing the reform at the end of 1999 (or beginning of 2000).

The Ministerial Conference held in November 2001 in Doha, Qatar launched the first round of multilateral trade negotiations after the establishment of the WTO. The Doha Declaration provides a new mandate for negotiation on a range of subjects, including agriculture and service negotiations starting from early 2000. According to the Doha Work Program, the agricultural negotiation is conducted under three pillars-domestic support, export competition and market access. And the major objectives of the negotiation in this round as agreed by the Members are as follow: “improvements in market access; reductions of, with a view to phasing out, all forms of export subsidies; and substantial reductions in trade-distorting domestic support.”<sup>37</sup>

#### 4.1.1 The development of negotiations

The negotiations have undergone several phases: (i) “Early Phase” from early 2000 till March 2002; (ii) “Preparation of Modalities” from March 2002 to July 2003; (iii) “the Cancun

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<sup>36</sup> Lamy, Pascal (2008), WTO chief raps US, EU on Doha Round trade talks, Xinhua News Agency. May 30, 2008.[http://news.xinhuanet.com/english/2008-05/30/content\\_8281486.htm](http://news.xinhuanet.com/english/2008-05/30/content_8281486.htm). [Accessed September 25,2008]

<sup>37</sup> WTO (2001), *Doha Declarations*, 20 November 2001. Published by the WTO Secretariat. p. 15

and July Framework Phase” from August 2003 to August 2004; (iv) “Modality Phase” from September 2004 to July 2008.

The first phase consisted of submitting and discussing proposals containing Members’ initial positions, lasting from early 2000 to March 2001. The following year was filled with informal meetings and non-paper proposals. As stipulated in the Work Program, the modalities for the actual negotiations were to be established no later than 31 March 2003. Members then began to prepare for the modalities to be submitted to the Cancun Ministerial Conference in September 2003. However, negotiators missed that deadline for producing elements including targets and formulas to reach modalities. The failure of the Ministerial Conference in Cancun also cast a shadow on the future of the agricultural trade talks. However, a last minute effort from the major Members by the end of July 2004 guaranteed the prospect of negotiations in the form of the so-called “July Framework”.

Since then, the negotiations went into the modality phase, which should in turn be used to work out the final agreement on revised rules, and individual countries’ commitments. The negotiations after then went slowly in spite of the effort made by the Members under chairperson of agriculture negotiations Tim Groser (New Zealand). The sixth Ministerial Conference held in Hong Kong, China in December 2005 achieved modest progress on the export competition: Members at that meeting agreed to phase out export subsidies by the end of 2013. They also agreed to establish modalities in agriculture negotiations by April 30, 2006. However, this deadline was missed this time again. Basically speaking, the deadlock of negotiations focused on a triangle of key issues: industrial and agricultural market access and domestic support.

In June 2006, the new chairperson Ambassador Crawford Falconer (New Zealand) put forward his draft modality (TN/AG/W/3), expecting that Members could reach consensus before the summer break. However, the position gap between developed countries led by the U.S and the EU and developing countries like Brazil and India were too wide to bridge. The General Council, at its meeting on 27-28 July 2006 approved the recommendation from the Director-General Pascal Lamy to suspend the Doha negotiations. After months of reflection and informal talks, at the support of Members, Pascal Lamy proposed the formal resumption

of negotiations in February 2007<sup>38</sup>. Ambassador Falconer then submitted two sets of challenge papers in the following April and May and submitted to Members another draft modality paper (TN/AG/W/4); however, only limited progress was achieved. The Members continued their intensive negotiations from September 2007, trying to conclude the negotiation by the end of 2008. Ambassador Falconer revised the draft modality paper twice, and the latest version was distributed on 10 July 2008 (TN/AG/W/4/Rev.3). However, Members again failed to reach consensus on the draft modality in the following mini-ministerial conference held in July. On 11 August 2008, the chairperson circulated a report on the latest developments in the talks.

#### 4.1.2 The status quo of the domestic support

With a view to achieving substantial reduction in OTDS, the 2004 July Framework provides that the base level of overall trade-distorting domestic support (OTDS), as measured by the Final Bound Total AMS plus permitted *de minimis* level and the level agreed for Blue Box payments will be reduced according to a tiered formula (meaning bigger spenders reduce more). The July 2008 proposal further requires Members with AMS commitments to reduce their AMS substantially through a tiered approach; it also proposes that the product-specific AMS (PS-AMS) should be capped at a certain (historic) level. Finally, in order to achieve the required level of cut in OTDS, Members may also have to cut their *de minimis* and blue box support levels.

The basic structure of the chairperson's draft modality paper was formed in this order, with changes on numbers and precision in language. The chairperson's draft modalities paper released on 10 July, 2008 reflected the latest thinking among negotiators and chairperson, with a view to preparing for the mini-ministerial conference later that month<sup>39</sup>. According to that paper, the base level of OTDS is equal to the Final Bound total AMS plus 10 percent of the average total value of the agricultural production in the 1995-2000 base period, plus the higher of notified blue box payments and 5 percent of the average value of production in the same period. Because the US did not notify domestic support measures as blue box, the blue box base level equals 5 percent of the average value of agricultural production in the

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<sup>38</sup> WTO (2007), 'Lamy: we have resumed negotiations fully across the board'. *WTO 2007 News Item*. 7 February, 2007. [http://www.wto.org/english/news\\_e/news07\\_e/gc\\_dg\\_stat\\_7feb07\\_e.htm](http://www.wto.org/english/news_e/news07_e/gc_dg_stat_7feb07_e.htm). [Accessed August 20, 2008]

<sup>39</sup> WTO (2008). *Revised draft modalities for agriculture*. Special Session, CoA.TN/AG/W/4/Rev.3. July 10, 2008.

1995-2000. Therefore, the OTDS base level of the US in the 1995-2000 base period is 48,223.7 million dollars.

Table 8: Total value of US Agricultural Production during 1995-2007

Value of Agricultural Production during 1995-2000 (mill. US dollars)							
Year	1995	1996	1997	1998	1999	2000	Ave. level
	190,110	205,701	203,884	190,886	184,735	189,520	194,138
Value of Agricultural Production during 2001-2007 (mill. US dollars)							
Year	2001	2002	2003	2004	2005	2006	2007
	198,502	194,572	216,478	235,688	236,001		

Source: G/AG/N/USA/10, 17, 27, 36, 51, 60.

The modality paper further provides the reduction rate, implementation period and staging of the OTDS, AMS, *de minimis* and blue box. One of the main reasons causing the deadlock in agriculture and the whole negotiations is the reduction rate in OTDS for the US. The G20 requires the US to reduce its OTDS by 75%, while the US offer is far beyond their expectation. Even though the USTR Schwab showed the willingness to accept the new OTDS of \$14.5 billion at July 2008 Ministerial Conference, the developing countries were yet not satisfied with that.

According to the modality paper, the reduction for the US will be 66% or 73% of the OTDS base level and the reduction shall be reduced by one-third on the first day of implementation. The remaining reductions shall be implemented annually in five equal steps. If this proposal is agreed, the US will reduce its OTDS level from \$ 48.22 to \$16.4 or \$13.1 billion, and the US has to reduce \$16.1 billion on the first day of implementation.

For the reduction of final AMS, the reduction for the U.S will be 60% of the Final Bound AMS in the Uruguay Round, and the cut will be implemented by 25 percent on the first day of implementation, followed by reductions in equal annual installment over five years. According to the proposal, the final AMS level for the US will be \$7.6 billion, substantially lower than the average usage of AMS during 2001-2005 as shown in Table 4 (\$11.1 billion). The significant element for the US on AMS reduction is the capping of PS-AMS, which is slightly different from other developed countries. For the U.S, the limits for the PS-AMS will be the resultant of applying proportionately the average product-specific AMS in the [1995-2004]

period to the notified average product-specific total AMS support for the 1995-2000. There are two points which need to be emphasized: first, if the US has introduced PS-AMS above the *de minimis* level while it did not have that in the base period, the limit for the PS-AMS will be the average amount of such PS-AMS support for the recent two years prior to the adoption of modality. For example, the US did not provide support to chickpeas during 1995-2000 period while providing support in recent years, then the PS-AMS for chickpeas is the average of the support in the recent two years (0.228 million dollars). The same situation applies to lentils and dry peas. Second, if the PS-AMS for each year during the base period was below the *de minimis* level, the PS-AMS will be capped as the amount of *de minimis* level. For instance, the support provided to rye during 1995-2000 did not exceed the average *de minimis* level at that period, so the PS-AMS limit for rye will be that *de minimis* level (1.4 million dollars). The capping for PS-AMS will be fully implemented on the first day of implementation period, except when PS-AMS in the two most recent years is higher. Blanford, Laborde and Martin (2008) have made detailed analysis on the PS-AMS limits based on the chairperson's draft paper released May 2008, where every single limit for the PS-AMS can be found.

Table 9: Product-Specific AMS limits for the US under the Modality Paper  
(Chairperson's draft modality paper in May 2008)

	Base (million dollars)	Year 1	Year 2	Year 3
Apples	76.588	76.588	76.588	76.588
Apricots	1.813	1.813	1.813	1.813
Avocados	0	0	0	0
Barley	35.636	32.895	30.153	27.412
Beef and Veal	1,254.76	1,254.76	1,254.76	1,254.76
Blueberries, wild	1.785	1.785	1.785	1.785
Cattle and calves	1,255.38	1,255.38	1,255.38	1,255.38
Chickpeas	0.228	0.228	0.228	0.228
Corn	1,438.38	1,327.73	1,217.09	1,106.44
Cotton	1,476.99	600.399	142.495	142.495
Cranberries	10.717	10.717	10.717	10.717
Dairy	4,905.90	4,864.22	4,822.54	4,780.85
Dry peas	34.771	34.771	34.771	34.771
Grapes	131.175	131.175	131.175	131.175
Hogs and pigs	512.837	512.837	512.837	512.837
Honey	2.891	2.891	2.891	2.891

Lentils	6.126	6.126	6.126	6.126
Livestock	1,255.38	1,255.38	1,255.38	1,255.38
Lychee	0.232	0.232	0.232	0.232
Canola	15.119	15.119	15.119	15.119
Crambe	0.002	0.002	0.002	0.002
Flaxseed	0.041	0.041	0.041	0.041
Mustard Seed	0.105	0.105	0.105	0.105
Rapeseed	0.026	0.026	0.026	0.026
Safflower	0.538	0.538	0.538	0.538
Sesame	0.011	0.011	0.011	0.011
Sunflower	35.544	35.544	35.544	35.544
Mohair	3.136	3.136	3.136	3.136
Oats	9.415	9.415	9.415	9.415
Olives	2.941	2.941	2.941	2.941
Onions	35.135	35.135	35.135	35.135
Orchards & vi- neyards	798.187	798.187	798.187	798.187
Peaches	21.979	21.979	21.979	21.979
Peanuts	249.19	249.19	249.19	249.19
Pears	14.034	14.034	14.034	14.034
Pecan trees	11.707	11.707	11.707	11.707
Potatoes	133.431	133.431	133.431	133.431
Rice	313.677	313.677	313.677	313.677
Rye	1.405	1.405	1.405	1.405
Sheep and lamb	7	7	7	7
Sorghum	55.378	51.118	46.858	42.598
Soybeans	1,123.72	1,123.72	1,123.72	1,123.72
Sugar	1,240.56	1,202.38	1,164.20	1,126.01
Tobacco	142.923	142.923	142.923	142.923
Tomatoes	86.202	86.202	86.202	86.202
Wheat	231.385	231.385	231.385	231.385
Wool	10.095	10.095	10.095	10.095

Source: Blanford, Laborde and Martin (2008).

With regard to the reduction of *de minimis*, the reduction will be no less than 50 percent on the first day of the implementation period. Meanwhile, additional effort may be undertaken to meet the objective of OTDS commitment.

With regard to the blue box, the proposal permits the United States (although not specified) to move its domestic support from AMS to blue box on certain conditions. The modality

paper capped the maximum blue box limit at 2.5 percent of the average value of production during the base period of 1995-2000, which is applied from the first day of implementation. For the US, the overall blue box limits will be \$4853.5 million. Similar to the amber box, a limit for product-specific blue box (PS-blue box) is also established, where the US again is likely to obtain special treatment. For the U.S, the limit will be [(110) (120)] percent of the average product-specific amounts resulting from applying proportionately the legislated maximum permissible expenditure under the 2002 Farm Bill to the overall Blue Box limit of 2.5 percent of the average value of agricultural production during the 1995-2000 period. Nevertheless, the limit may be exceeded only where there is a corresponding and irreversible one-for-one reduction for the products concerned in the product-specific AMS limits (the rate for cotton is two-for-one). Meanwhile, another flexible treatment under paragraph 47 could theoretically provide an additional loophole for the US; however this is probably not feasible in reality. The modality paper provides that, if no product-specific entitlement to a Blue Box limit and no current AMS support in the base period exist, and if the total support for this product does not exceed 5 percent of the overall blue box limit, then product-specific blue box limit may be 2.5 percent of that overall limit.

The possible blue box limit for the US and for a single product is as follows:

Table 10: Product-Specific Blue Box limits for the US in the Modality Paper

Crop	Average maximum payment during 2002-2007(mill. dollar)	Percentage of total payment	PS-blue box limit	
			110%	120%
Corn	3,224.20	44.20%	2359.74739	2574.2699
Sorghum	147.4	2.00%	106.7759	116.4828
Barley	46.7	0.60%	32.03277	34.94484
Oats	8.7	0.10%	5.338795	5.82414
Wheat	1,421.50	19.50%	1041.06503	1135.7073
Soybeans	550.3	7.50%	400.409625	436.8105
Cotton	1,376.50	18.90%	1009.03226	1100.7625
Rice	323.1	4.40%	234.90698	256.26216
Peanuts	200.9	2.80%	149.48626	163.07592
Total	7,299.20	100.00%	5338.795	5824.14

Source: WTO (2008).

Considering the importance of cotton issues, the reduction of amber box and blue box ceilings is deeper for cotton than for other agricultural products. According to the proposal,

the US has to reduce 82.2% of its arithmetic average of AMS support during 1995-2000, and the implementation will be one third of the implementation period. And the PS-blue box limits will be one third of the limits above. According to this author's simulation, the base level of cotton support will be reduced from \$800.5 million to only \$142.5 million in two years.

Table 11: AMS reduction for cotton of the US in the Chair's Modality Paper

Year	Base level during 1995-2000(mill. dollar)	Year 1	Year 2	Year 3
Reduction	-	25%	82.2%	-
Amount	800.5	600.4	142.5	142.5

Source: WTO (2008).

## 4.2 Program support of 2008 Farm Bill under Falconer's text

Generally speaking, unlike for agriculture market access, the US has its most defensive interest in the pillar of domestic support, so the imposition of additional WTO disciplines on domestic support is the biggest single issue for the United States. In order to evaluate the effect of the chairperson's paper on the implementation of the 2008 Farm Bill, there are several other factors to be taken into account: (i) the implementation period of a possible Doha deal; (ii) the evolution of worldwide commodity prices; (iii) the political climate in the US

### 4.2.1 Implementation period between possible Doha Deal and 2008 Farm Bill

Since the commencement of the Doha round in November 2001 Members have established for themselves numerous timetables by which to conclude the round. This author joined the negotiation team for a couple of years, and witnessed words like "deadline" appearing several times. During the last week of July 2008, Director-General Pascal Lamy repeatedly called on major members to play their leading role in carrying forward the negotiations. Despite his efforts, the prospects of the negotiations are not positive, a view which is shared by many senior officials and diplomats. The priority of the US in the future couple of months would be the election of the new president and the partial Congressional elections, which means the US will not pay as much attention to the negotiations as before. The view of the multilateral trading system of the new president and the new Congress may not be the same as now. In addition, France is chairing the EU until the end of 2008, implying that the political

commitment from the EU to the WTO will not be so strong, taking the conservative position of France into account. Supposing that the negotiations could resume late this year and Members could reach convergence over the modality paper, members still need to finish other negotiations such as services and rules to ensure the single undertaking package, which certainly takes more than half a year. After that, Members would have to prepare and negotiate their schedules of concessions. A final agreement on the Doha round would then need to be ratified by each Member. Accordingly, in my opinion, the earliest date to start implementing the Doha deal, if there is one, could be January 1, 2011. Meanwhile, we have to bear in mind that the 2008 Farm Bill has been in force since last June according to the USDA announcement<sup>40</sup>. Under these circumstances, the new Doha deal would affect the implementation of the 2008 Farm Bill for only one year at most.

#### 4.2.2 Impact on the commodity programs under the 2008 Farm Bill

Assuming that Members could reach a consensus on the proposals for the new domestic support disciplines in the chairperson's paper, the possible impact of the new commitment on the US will now be examined.

Needless to say, the reduction in the OTDS and the final AMS will constrain the room for maneuver for such US domestic support as is most closely linked to prices. As has been mentioned above, if the provision on the reduction of OTDS in the final Doha deal is the same as in the chairperson's modality paper, the final level of OTDS will be bound at 13.1 or 16.4 billion dollars after the implementation period, compared to the base level of 48.2 billion dollars. The total AMS and AMS for cotton would be 7.6 billion and 142.5 million dollars, significantly reduced compared to the base level of 19.1 billion and 800.5 million dollars. However, the average level of OTDS for the US during 2001-2005 was 18.2 billion dollars, and the figures in 2006 and 2007 will be less than that due to increased commodity price. In other words, the reduction of OTDS and AMS will only squeeze out the water of the US policy space, without obliging the US to reduce present payment levels. Orden, Blanford and Josling (2008) have also supported this statement by predicting that (under present price trends) the

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<sup>40</sup> USDA (2008), 'USDA Delivers First Action for New 2008 Farm Bill: Schafer Announces Crop Loan, Ldp Provisions and Loan Rates'. 2008 Farm Bill News Release. June 18, 2008.  
[http://www.usda.gov/wps/portal/!ut/p/\\_s.7\\_0\\_A/7\\_0\\_IOB?contentidonly=true&contentid=2008/06/0156.xml](http://www.usda.gov/wps/portal/!ut/p/_s.7_0_A/7_0_IOB?contentidonly=true&contentid=2008/06/0156.xml) [Accessed September 15, 2008]

new OTDS limit will not be binding for the US even after the end of the implementation period<sup>41</sup>.

One of the important issues is the limit set up for the product-specific AMS. During the 1995-2004, the US has notified 46 commodities with AMS support for at least one year. According to the provision on the PS-AMS, those commodities would be subject to the new PS-AMS limits. However, based on the U.S notifications, the major recipients of the domestic support are dairy, corn, cotton, sugar, soybeans, rice, peanut and wheat, which covers about 97 percent of the annual AMS support during 1995-2004 (as shown in Table 11).

Table 12: Composition of the AMS used by the US during 1995-2004

Crops	Average AMS outlays (million dollars)	percentage
Dairy	4,857.18	45%
Corn	1,423.95	13%
Cotton	1,190.37	11%
Sugar	1,142.76	11%
Soybeans	1,036.40	10%
Rice	300.02	3%
Peanuts	236.88	2%
Wheat	214.47	2%
Other products	10425.03	3%
Total annual AMS	10,725.00	

Source: WTO notifications.

Considering the support concentration in the US subsidy system, the PS-AMS limits for the major crops are of additional importance. Those eight crops are eligible for direct payment, CCPs, marketing assistance loans and the newly-created ACRE program. If the new ACRE program is not taken into consideration, the direct payments for the major crops will be as follows:

Table 13: Possible Amount of Direct Payment for the US during 2008-2012

Crops	Base acre	DP yield	DP rate	DP amount (mill. dollar)	
	million acres	bushel/acre		2008	2009-2012
Wheat	74.8	34.5	\$0.52/bu	1140.6	1117.8
Corn	86.76	102.4	\$0.28/bu	2114.4	2072.2
Cotton	18.4	599	\$0.0667/lb	624.9	612.4

<sup>41</sup> Orden, David, Blanford, David and Josling, Timothy (2008), Determinants of Post-Uruguay Round US Farm Policies. Presented at the *World Bank Conference on Political Economy of Distortions to Agricultural Incentives*. Washington DC, USA. May 23-24, 2008. p.37.

Rice	4482.8	4819	\$2.35/cwt	424.0	415.5
Soybean	52	30.8	\$0.44/bu	599.0	587.0
Total				4902.9	4804.9

Source: 2008 Farm Bill and USDA (2008).

As has been mentioned in previous chapters, the direct payment has already been scrutinized under the DSB. If the US notifies direct payment as non-product-specific AMS measures, this amount will not possibly exceed 5 percent of value of agriculture production. If the direct payment is to be qualified and notified as product-specific measure, the large amount of subsidies under direct payment will constitute problems for the US. If the US persists in notifying them as a green box measure, there could be new trade disputes in the future.

Although the US has not used the blue box measure in the past years, it is widely recognized the US would like to notify the CCPs in the future as the blue box to reduce its notification pressure. The maximum legitimate expenditure under the CCPs of the new bill will exceed the product-specific blue box limits for the crops including wheat, corn and soybean. If the US wants to classify the CCPs as blue box, it needs to reduce its AMS limits for the products concerned. The required AMS reduction is as below:

Table 14: Relations between AMS reduction and PS-Blue Box limits

Crops	PS-AMS limit	Maximum CCP	PS-Blue box limits		Required AMS reduction	
			2010-2012	110%	120%	110%
Wheat	231.4	1629.6	1041.1	1135.7	588.5	493.9
Corn	1106.4	3374.6	2359.7	2574.3	1014.9	800.3
Cotton	142.5	716.1	336.3	366.9	759.6	698.4
Rice	313.7	322.4	234.9	256.3	87.5	66.1
Soybean	1123.7	844.2	400.4	436.8	443.8	407.4

Source: 2008 Farm Bill and USDA (2008).

If so, no matter whether the option is 110% or 120%, the US would have no problem for corn, rice and soybean, while wheat and cotton would exceed the AMS limit. However, if the direct payment is also notified as PS-AMS measure, then the situation will be worsened, i.e., corn, wheat, cotton and rice will exceed their own PS-AMS limit. Blanford, Orden and Josling (2008) projections further shows that the AMS binding would be operative for dairy and sugar during the whole implementation period, and the blue box binding is exceeded by a major amount for cotton during all years of the implementation period. Their projection also predicts that the cotton blue box binding will be exceeded during the whole implementation

period.

With regard to the other products, the actual notified support of 19 products in the past is so small that the PS-AMS limits will be at the *de minimis* levels during the base period of 1995-2000, which means that the chairperson's draft modality creates enough "policy space" for the US to provide subsidies. Those products include apple, apricots, beef and veal, cattle and calves, cranberries, grapes, hogs and pigs, sheep and lamb, livestock, lychee, olive, onions, orchard and vineyards, peaches, pears, pecan trees, potatoes, rye and tomatoes, the maximum amount of AMS support of which can be found in Table 9. Meanwhile, most of those products are not covered under the commodity provisions in the 2008 Farm Bill. In other words, the chairperson's draft paper creates possibilities for the US to "legitimately" subsidize those products. Even for eligible products for loan programs like wool, mohair, honey, chickpeas, dry peas, lentils and minor oil seeds, the possible maximum support limit does not constrain the implementation of the farm bill, according to the budget expenditures released by the USDA in February 2008. For wool and mohair, the PS-AMS limits after the Doha deal would be 13.2 million dollars, while the possible government subsidies at the same time would only be 8 million dollars.

However, it needs to be pointed out that those simulations by Blanford, Orden and Josling (2008) are based on extremely low levels of commodity prices. The reality, instead, is that commodity prices are soaring. According to latest USDA simulation, the CCP payment amount to farmers in the next six years will be zero. In this case, the US would have no problem at all to meet the new commitments – but the new WTO limits would also limit future spending increases in case of a price turnaround.

As many scholars have mentioned, due to the introduction of the newly-built ACRE program under 2008 Farm Bill, the assessment of the possibility that whether the US would exceed the caps with the new Doha deal is relatively complicated. It is still unknown how many farmers will join the new program, so the impact of the new Doha deal on the 2008 Farm Bill remains to be seen in the near future.

#### **4.3 Will the US Administration accept Falconer's text?**

*"Today I broaden the challenge by making this pledge: the United States is ready to*

*eliminate tariffs, subsidies and other barriers to free flow of goods and services as other nations do the same... It's the key to overcoming poverty in the world's poorest nations. ...By expanding trade ...we strike a blow against the terrorists who feed on anger and resentment.*<sup>42</sup>” (George W. Bush)

After the establishment of the WTO, the plan to initiate a new multilateral trade negotiation was put forward; however, this plan did not gain much support from the major groups particularly the US where a first attempt failed in the Seattle Minister Conference in 1999. However, the impact of the September 11 terrorist attacks gave impetus to it. The US thought that poverty in the developing world was at the root of terrorism, and a better standard of living would help reduce the threat of terrorism. Therefore, the US turned to fully supporting the commencement of a new round, and two months later the Doha Round was launched in the capital of Qatar (November 2001).

From the very beginning of this round, the US has been a major player in negotiations as it was in the past. It must be underlined that the final result of the Doha round negotiation is a single-undertaking package, which means nothing is agreed until everything is agreed on a consensus base. In other words, the negotiations progress on agriculture, NAMA, Services, TRIPs, rules or any other topics will play an important role in successfully concluding this round or possibly blocking the final deal.

In the area of agriculture negotiation, the priority for the US is to expand their agricultural exports through an ambitious reduction of tariffs, because the average tariff in the US is significantly lower compared to the high average level in many other markets. Even in the sensitive area of domestic support and export competition, the present US Administration wants to support its farmers in a more WTO-consistent way, and to diminish budget deficit and defend its credibility to the multilateral trading system.

For most developing countries, one important element to assess the so-called “development agenda” is whether the farm subsidies provided by rich countries could be substantially reduced. At the same time, the imposition of tighter WTO disciplines on domestic support means that the US needs to take more effort and possibly modify some of its major domestic

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<sup>42</sup> Bush, G. W (2005), Speech Delivered at the United Nation General Assembly Meeting, September 14, 2005. <http://www.un.org/webcast/summit2005/statements/usa050914eng.pdf>. [Accessed August 20, 2008].

farm programs. From the perspective of developing countries, the US agriculture sector is largely government-funded and a reduction of subsidy certainly will diminish or even eliminate the farmers' support of the government, an important power in US politics. Although the Administration looks forward to a balanced budget in the next few years, the government and parliament are reluctant to take the risk of offending large domestic interest groups, unless they could get equivalent benefits for those groups in return. We have witnessed twice that the Administration rejected the modality paper on agriculture in the past two years, which gained huge support and applause from the Congress.

Will the US accept the chairperson's latest modality paper on domestic support? Technically speaking, it may not constitute a major problem in view of their actual spending levels on agriculture; however, it could be a huge political issue because it would seriously limit the spending capacity of Congress. Even before the mini-ministerial conference in last July, the main drafter of the 2008 Farm Bill, Senator Tom Harkins together with his colleagues, wrote a letter to the USTR to express their concern over decisions that could impact domestic producers and requested the USTR to reject an unbalanced outcome<sup>43</sup>. Finance Committee Chairman Max Baucus also urged the Administration to resist any trade deal that does not provide meaningful market access for US exporters<sup>44</sup>.

Anyhow, the negotiations collapsed, apparently due to the wide differences on the special safeguard mechanism (SSM) in farm products for developing countries, whereas the key issue of domestic support, particularly cotton, was not even discussed. According to Senator Harkins, the chairperson paper's provisions on sensitive products, special products, SSM and exceptions for the recently-acceded members do not inspire much confidence on the definition of "balanced"<sup>45</sup>.

It is expected that the US will reject whatever draft modality paper again, unless the requests from the Congressmen mentioned above could be resolved. The official US position remains unchanged: as many senior US government officials have implied numerous times, the US is ready to make meaningful changes to American farm programs, provided that other countries offer tangible market access for major US agricultural exports.

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<sup>43</sup> Harkins, Tom (2008), '*Senators urge balanced Doha round trade agreement in advance of ministerial in Geneva*'. Letter to the USTR, July 17, 2008. <https://harkin.senate.gov/pr/p.cfm?i=300979>. [Accessed July 20, 2008]

<sup>44</sup> Baucus, Max (2008), *More market access needed to gain congressional support for Doha Round*, Letter to the USTR, 29 July, 2008. [http://insidetrade.com/secure/pdf12/wto2008\\_4520.pdf](http://insidetrade.com/secure/pdf12/wto2008_4520.pdf). [Accessed September 10, 2008]

<sup>45</sup> Harkins, Tom (2008), *ibid.*



## **Chapter Five: Outlook**

### **5.1 2008 Farm Bill: Stumbling block or Building Block?**

The US farm subsidy system has long been recognized as a major stumbling block in global trade negotiations. Many people hoped for major reforms in the new farm bill, and certainly the Administration tried to at least avoid more problems for the US position in the WTO negotiations, and in dispute settlement. However, when the 2008 Farm Bill was passed, the mainstreaming view is that the farm bill has landed like an unwelcome guest at the negotiating table.

There is no denying that the passage of the subsidy-laden election year bill foreshadows a slimmer margin of maneuver for the administration in the WTO negotiations on agriculture. The farm bill has generated domestic critics, because it just heads in the wrong direction in terms of the US international obligation. As mentioned above, the US would like to expand their share in the world agriculture market, particularly the markets of the emerging economies, and the US offered the reduction of domestic subsidies in exchange for such market access. For the rest of the world, particularly the developing world, the US farm programs have significant adverse impact on their agricultural production, because they can't compete against the farm subsidies. Therefore, they expected to change this imbalance through multi-lateral forum. However, due to the powerful domestic lobby, the US farm policy reform effort did not achieve its goal and will even increase the subsidies to many crops.

After several years of tough negotiations, the Doha round has come to a critical juncture. The momentum gained in the past few months had signaled the possibility to finalize major issues this year. However, the negotiation collapsed in July 2008. The new bill not only hampers the US effort and credit in agriculture trade reform, but squandered the chance to reach a pro-development deal. The failure to reach convergence on SSM is the direct fuse to cause the collapse of trade talks; however, the root was still the commodity program under the farm bill. Developing country members are worried that the continuation of large subsidies in 2008 Farm Bill will enable the US farmers to expand their production, which would in turn damage the local production with less or no subsidy at all in developing countries. Under this condi-

tion, it is unreasonable for them to show further flexibilities on the SSM, which may protect them from damage caused by the import quantity surge or price decrease due to subsidies from the US

A final collapse of the Doha trade talks would be another blow to the struggling world economy, and there's plenty of blame to go around, among which the US farm bill. In my opinion, most people except the US farmers are not happy with the commodity provisions under the Farm Bill, because it missed another opportunity to expand world trade and enhance development. However, could this stumbling block turn into the building block? It needs to be emphasized that there is a separate provision on the administration of commodity programs under the 2008 Farm Bill, and any determination made by the USDA Secretary is final and conclusive. If the Secretary determines that expenditure under international agreement exceeds the allowable levels, he/she could make adjustments in the amount of expenditure to make sure that such expenditure does not exceed that level. In other words, even though the farm bill authorizes the USDA to implement the farm bill with 35 billion dollars, the Secretary could have his own discretion to decide and stop distributing money to farmers. In this context, the US could just offer to reduce its expenditure under the new farm bill to get serious concessions from other countries in return.

Compared with previous multilateral trade negotiations, the Doha agriculture negotiations have achieved much progress, on the elimination of export subsidies and even the reduction of tariff and subsidies. Even the lock-in of the current negotiation results could more or less improve the competition conditions in the world market.

A review of the Presidential candidates' attitude toward the farm bill reveals that the Democratic presidential contender Barack Obama welcomed the bill's passage<sup>46</sup>, while the Republican nominee John McCain called it a bloated piece of legislation that will do more harm than good for most farmers and consumers<sup>47</sup>. Even so, we are not sure whether either of the candidates will support a possible trade deal based on the existing proposals or try to enforce a completely different one. In this way, it is better for the developing countries to lock in what has been agreed now rather than let negotiations drag on to an uncertain future.

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<sup>46</sup> Obama, Barack (2008), 'Obama Statement on Passage of the Senate Farm Bill', *Obama News*, May 15, 2008. [http://www.barackobama.com/2008/05/15/obama\\_statement\\_on\\_passage\\_of.php](http://www.barackobama.com/2008/05/15/obama_statement_on_passage_of.php). [Accessed September 15, 2008]

<sup>47</sup> Abbott, Charles (2008), 'McCain agrees with Bush on farm bill veto'. *The Reuters News*. May 19, 2008. <http://www.reuters.com/article/vcCandidateFeed7/idUSN1955821320080519>. [Accessed September 15, 2008]

## 5.2 The 2008 Farm Bill and the Chinese Economy

In spite of its name as legislation governing domestic farm policy, the impact of this legislation goes far beyond domestic industry, and the farm bill could even play a significant role in affecting China's economy.

### 5.2.1 China's agriculture sector

In my opinion, among the bilateral economic relations in the world, the relationship between China and the US would be the most complicated bilateral relations in international arena.

Like the US, China is also an important character in the world agriculture market: it is the largest producer, fifth agricultural exporter and fourth importer of agricultural products. Although China has a trade surplus in general over the US, it has a huge trade deficit on the trade of agricultural products. According to MOFCOM, China's import from the US has surged from 2793 million dollars in 2001 to 9125.8 million dollars in 2007, while the export has just increased from 1260 to 4383.8 million dollars. And it is projected that the figure will continue to rise. It is important to know that China's major imported agricultural products from the US are soybeans, cotton, wheat, corn, chicken and hide, which are the main recipients of US government subsidies.

The implementation of the 2008 Farm Bill will not only hamper China's export of competitive agricultural products, but also aggravate China's development in a weak sector. The increase of payment rate on most commodity programs will further reduce American farmers' production cost and stimulate domestic production, which will in turn help the US gain more share in world trade through the price advantage deriving from the subsidies. According to the FAO, China and the US are ranked as the sixth and fourth largest rice exporters<sup>48</sup>. The price advantage from subsidies will help the US export rice at the subsidized price that Chinese rice can't compete against. Moreover, the subsidies will increase China's import and thus worsen the development of those sectors such as dairy, sugar and soybean. For example, China has

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<sup>48</sup> FAO (2007), *Food Outlook 2007*, Global Market Analysis, Food and Agriculture Organization. November 2007. <http://www.fao.org/docrep/010/ah876e/ah876e05.htm#33>. [Accessed September 12, 2008]

become the largest destination for the US soybean export, and the quantity has reached 115.7 million tons. Meanwhile, the soybean production in China has been decreasing, one of the important reasons being the local farmers are unable to compete with the cheaper imported soybean.

In sum, the implementation of the new bill will increase the uncertainty that China's agriculture will face and worsen the competition conditions in international market.

### 5.2.2 Other Chinese Industry sectors

In contrast to the farmers, other Chinese industry sectors have been the indirect beneficiaries of the US subsidies granted to crops.

The whole world is surprised and even a little frightened by the development of China's textile sector. However, most people are not aware of the fact that the US has been the major exporter of cotton to China, which has increased from 48.4 thousand tons in 2001 to 112.4 million tons in 2007<sup>49</sup>. China is also an important cotton producer, but the local production can't meet the huge demand from the textile sector. Meanwhile, the quality of US cotton is another important factor besides cheaper prices. In other words, the subsidies provided by the US government to its farmers have then transferred to the hands of Chinese producers, although in fact the Chinese manufacturers take a little percentage of the final value. A similar story applies to the bakery industry as well.

Even in the case of soybean, the story is different from the perspective of consumers. The average take-in level of vegetable oil in China is still far below the world average level. Meanwhile, due to the limitation of arable land, it is not reasonable for the farmers to use their land to plant soybean. The imported soybeans are mostly used to process soy oil, which is the main source of edible oil in China particularly rural areas. In this way we can say that the US government is partly paying for the Chinese consumers of soy oil.

## 5.3 Should China bring 2008 Farm Bill implementing measure before DSB?

Since its accession into the WTO, China has been actively participating in the dispute settlement: mostly in the form of third parties, five times as respondent and once as complainant.

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<sup>49</sup> The Author's calculation based on internal statistics.

nant. There have been scholars calling for the government to sue the US subsidy programs before the WTO, particularly after Brazil successfully challenged the US cotton subsidies in 2004.

From the technical level, there are conflicts between the US farm policies and the WTO obligations. The direct payment and counter-cyclical payment authorized in the farm bill have been proved to be inconsistent with WTO rules, and Brazil and Canada also claim that the US is in violation of its WTO commitment on domestic support. In addition, the 2008 Farm Bill does not change the fundamental system of domestic support. It is expected that more Members may resort to the DSB, particularly after the collapse of the negotiations.

However, the decision may be influenced by many uncertainty factors. The trade dispute normally takes at least two years, and arbitration and implementation need more time. The lengthy time period for a dispute will reduce the economic value of the case, and the WTO does not support compensation for past damage. What's more, the increasing commodity prices reduce the average applied level of subsidies, because the US subsidies are market price linked. Moreover, the Secretary of USDA has the discretion to stop paying out, if he believes the paid amount is exceeding the US commitment. In addition, the economic relationship with the US has been given high priority, and the Chinese government normally prefers bilateral dialogue or consultations rather than a multilateral mechanism to resolve their disputes, unless the bilateral method is ineffective. Since China's accession into the WTO, China has only initiated two cases before the DSB against US trade measures: the Steel safeguard case along with six other countries and the Coated-free Sheet Paper case in 2007. However, trade protectionism has gained some support in the US due to the economic slowdown and huge deficit to China and the US has filed four dispute cases against China in the year 2007, which caused many critical voices in Chinese academia. Under this condition, it is possible for the Chinese government to sue the US trade measure and to fight back. Moreover, defending the farmers' interests will send them a positive signal to encourage their production, which could help build the confidence and credit of the central government.

In conclusion, the 2008 Farm Bill has a detrimental effect on the Doha round agriculture negotiations, but it could turn out to be the building block if the Members eagerly press for the lock-in of existing progress and early conclusion of this round. Meanwhile, the US subsi-

dies provided to its farm sector have a combined effect on Chinese economy. Challenging the US before the WTO is not only a mere economic issue, but also of political dimensions in China. In order to make that decision, the Chinese government has to carefully weigh the political and economic benefits and cost.

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