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# **THE EU APPROACH CONCERNING AGRICULTURE IN THE NEXT WTO ROUND**

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## **The EU Approach Concerning Agriculture in the Next WTO Round**

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### **1. Introduction**

Agriculture becomes more and more crucial in keeping world trade relations on a firm basis. The present paper aims to give a broad outline of the main agricultural issues expected to be raised in the framework of the multilateral trade negotiations under the next WTO round. Since the EU represents one of the principal actors in the world agricultural trade, it is believed that the EU position on these issues will affect not only the content but most probably the outcome also of the negotiations. This paper will try to present the EU approach in the forthcoming negotiations in relation to the priorities identified and set recently by the EU.

### **2. The CAP and the GATT: A difficult coexistence**

There is no doubt that the Common Agricultural Policy (CAP) has become and still is the most important and most *comprehensive* common policy ever developed by the EU, at least in terms of integrity and budget. Since its establishment and inclusion in the initial Treaty of Rome, in 1957, the CAP succeeded in transforming EC in world markets from a net importer of agricultural products to a net exporter.

This success (and the criticism thereof) is attributed to the fact that under the CAP (and especially during its full operation up to 1992), a high level of support and protection has been applied for the European agriculture, based almost exclusively on a *price support mechanism* for the main agricultural commodities, which happen to participate extensively in the world trade.

For those who are not familiar with the issue and expecting that agricultural trade, as part of the overall trade, should in principle be subject to the original “General Agreement on Tariffs and Trade” (GATT), a reasonable question arises, how CAP (but also many other similarly protective policies applied by other States) could be established and even developed, since most of the basic policy instruments used, were clearly incompatible with almost all GATT rules and principles.

The answer lies to the fact that almost all the Contracting Parties took advantage of the various exceptions included into the GATT Agreement itself, with regard to the agricultural products, based either on permanent or on country-specific derogations (waivers).

In particular, the EC based the internal component of CAP on the disposition of Article XXIV (according to which the provisions (rules and principles) of GATT do not prevent the formation of a Custom Union or/and Free Trade Areas) and the external component on

- Article XI (concerning the general elimination of quantitative restrictions), which allows agriculture to be exempted from the prohibition of the use of non-tariff barriers (under certain conditions) and on
- Article XVI (on subsidies), which also offers possibilities (under certain conditions again but open to legal interpretations) either to grand or maintain any subsidy (including income and price support) or to grant export subsidies for agricultural products.

In general, all over the world, it was considered that the agricultural products could be excepted from the GATT rules and disciplines, for various reasons, having to do with the strategic choice of all the countries, especially after the tragic experiences of the II World War, to achieve *Food Security*. The “philosophy” behind it was that agricultural products were *not simply merchandises but mainly goods* necessary for the survival of the human being, justifying therefore a kind of “special treatment”.

However, all the years of operation of GATT, agricultural trade was a major source of permanent conflict between the big agricultural exporting countries (USA, Canada, Australia, Latin-American, etc.) and those countries that had being in big deficit of agricultural production and were trying to recover from the war (as it was the case of the European countries). For the first group, in particular, *liberalisation* should be a target for agricultural trade as well as it was accepted for the industrial products, and they repeatedly tried *to bring agricultural products under the general rules of GATT*. For the second group, however, other priorities, political, economic, social, structural, but also important historical, practical and technical reasons did not allow them to share the views of the first group. Among other things, the objections raised against the prospect of liberalising the agricultural trade were due, perhaps, to the fears that, apart of the rhetorics, the overall aim of the “liberalisers” (which were not seriously damaged by the last War) was in fact to take advantage of the initial difficulties for recovering and gain the maximum possible access to their food markets at a proper time.

### **3. The background – A brief overview**

Generally, the first seven Rounds of world trade negotiations that took place under GATT since 1947 did not achieve too much in the field of agriculture, due also to the fact that, in the years of big industrial expansion, their main focus was on the progressive reduction of tariffs in industrial rather than agricultural products. However, since its establishment, the CAP was always brought on the table of negotiations. In particular:

#### **3.1. Dillon Round (1960-61)**

The EEC participated for first time, as a single entity. The creation and inclusion of the CAP objectives into the Treaty of Rome prompted negotiations within the GATT (according to Article XXIV). At this early stage, the EEC accepted (as a counterbalance) lower duties on fruit and vegetables and (under article XXIV-6) offered *free market access* (zero tariff) for **3** arable crops: **soybean, cotton, oilseeds**. This binding concession was the origin of the crucial choice made by the EEC, in the process of establishing the CAP, *to exclude* these products (which operate in the food chain as substitutes of cereals in animal feed) from any price support measures.

#### **3.2 Kennedy Round (1964-67)**

It coincided with the establishment of the major Common Organisations of Markets under CAP (cereals, dairy products, beef) and, subsequently, with the first full implementation of CAP.

During the Round, the CAP came under attack by the US and also wanted *to abolish the system of variable levies in imports*. However, only marginal concessions were agreed (the EEC accepted a zero duty for **manioc** and **other cereal substitutes**). In a parallel negotiating procedure outside GATT, *the International Wheat Convention* was also concluded.

### 3.3. *The Tokyo Round (1973-79)*

Despite the fact that the Round took place under a very negative international economic environment (monetary instability, oil crisis, food shortages), once again, the CAP was at the centre of dispute. The US questioned the CAP basic mechanism (variable levies & export refunds). The final outcome of the Round on agriculture was largely determined by a bilateral EU-US compromise based upon a discipline on the use of export subsidies. In addition, the EU made *marginal* concessions on some products (**tobacco**, **hilton beef**, certain types of **cheese**). Two commodity agreements were also concluded under the auspices of GATT, establishing consultations for *bovine meat* and on *dairy products*.

## 4. The Uruguay Round Agreement on Agriculture (URAA)

Since 1986, when the Punta Del Este declaration launched the Uruguay Round, all the participants agreed to take on the task of *reincorporating agriculture into the GATT*, by promoting policy reform processes to the agricultural sector. However, the 113 Members of GATT were, broadly speaking, divided into two main groups of Countries, representing two opposite negotiating positions, *concerning the agricultural policies*:

On the one side, the US and the **15 of the Cairns group**<sup>1</sup> advocated mainly:

- The complete elimination of export subsidies within 5 years, and
- A substantial (75%) reduction in trade-distorting domestic support

That is, they advocated extremely *radical* reforms of the agricultural policies applied up to this time (and not only by EEC). In a short period (within 10 years), these reforms could lead to a *full liberalisation of the agricultural trade*.

On the other side, the **EU**, **EFTA**, **Japan** and most of the **food-importing developing countries** were opposed to such a liberalisation. They could favour, instead, limited reforms, only for those products that participated substantially in the world trade, by reducing domestic support at a level required to restore the equilibrium in the world markets.

The negotiating gap between the two groups dominated the 4-year discussions and, at the end of 1990, the Round did not succeed to reach an agreement (as it was initially scheduled).

The negotiations restarted at the end of 1991, on the basis of accepting separate commitments on three categories of policies:

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<sup>1</sup> The members of the group in alphabetical order: Argentina, Australia, Brazil, Canada, Chile, Colombia, Fiji, Indonesia, Malaysia, New Zealand, Paraguay, Philippines, South Africa, Thailand, Uruguay

- **Border Protection (Market Access)**
- **Domestic Support**
- **Export Competition**

It should be reminded that, it was the time when the 1992 reform of CAP was adopted which certainly changed the thrust of the UR negotiations.

Finally, a compromise was reached, between the two main actors (the EU and the US), in December 1992, in the so-called "**Blair House Agreement**" that allowed a final agreement to be reached in December 1993 and the "Final Act" to be signed in Marrakesh, Morocco, on April 1994.

In general, the commitments undertaken by the signatories of the **World Trade Organisation – WTO** (which replaced the GATT) under the URAA, should be implemented over a *6-year period*, starting in 1995 till the end of 2000, and by using as a *base or reference period* for the various measurements, mostly the average of 1986-88 of the relevant statistical data.

The most important, however, specific commitments in each of the above policy areas have, in brief, as follows:

#### ***4.1. Border Protection (Market Access)***

##### ***4.1.1. Tariffication***

The "tariffication" implies that all the non-tariff barriers (applied at the frontiers for agricultural products) should be converted into fixed tariffs, which, in turn, should be reduced by 36% on average, over the 6 year period.

From the point of view of CAP, this was perhaps the most important commitment undertaken under URAA. As a result of it, the **variable levies** (together with the **threshold prices**) which constituted, up to that time, one of the most essential mechanisms of CAP, disappeared. Therefore, one of the three fundamental principles governing CAP from the very beginning, that of "**community preference**", lost most of its significance. And this is because, even if the tariff equivalents are considered today too high, these levels are subject to gradual reductions at a **fixed** base (according to the GATT principle of tariff bindings). Given that the overall trade negotiations principally aim at tariff reductions in general, one should expect that tariffs, sooner or later, will continually decrease in the next successive Rounds, up to their elimination.

##### ***4.1.2. Safeguard Clause***

This clause, agreed initially in Blair House, is included into the URAA (Article 5) and provides a notable derogation from the principle of bound tariffs for all products. Under this clause, the Contracting Parties are allowed to temporarily apply additional duties (for products specified in their schedules of concessions) if **the quantity of imports** rises too quickly in relation to an average over the previous 3 years, or if **the import prices** fall more than 10% below a certain level ("trigger price"). In this sense, the safeguard clause, if applied, could be considered as the only remaining element of "variability" at the frontier protection.

It should be noted that the whole issue of the "safeguard clause" was agreed upon *the insistence of the EU* in URAA, as the EU tried to keep a "safety net" to avoid any market disturbances by excessive imports<sup>2</sup>. During the implementation period, however, other trade partners took also advantage of this clause<sup>3</sup>.

#### **4.1.3. Market access**

In relation to the previous "import quota arrangements", by converting levies and other non-tariff barriers into "**tariff rate quotas**", the signatories agreed to "regulate" the market access in respect to two components:

- a) The *current access component*, according to which the import tariff concessions granted before the agreement must be maintained *at least* at their 1986-88 levels (incorporating therefore, all the pre-existing import quota agreements), and
- b) The *minimum access component*, which provide access for additional imports by opening up market shares for third countries at least to 3-5% of the 1986-88 volume of consumption for each group of products.

The latter, however, should not be understood as an obligation to import. It is a granting of a *reduced custom duty* for this minimum quantity of imports. In this respect, there are two points to be raised:

- First, this commitment applies to the sectors *subject to tarrification* only. Therefore, for the EU, products like fruits & vegetables, wine, etc are excluded from this commitment, as they had not variable levies before the agreement to be tarrified.
- Second, the minimum access applies with regard to aggregation, that is, considering groups of products rather than isolated products. It should be noted that the "aggregation principle" was acceded to a EU insistent demand.

## **4.2 Domestic Support**

The commitment includes the obligation to reduce the general level of domestic support by 20% compared with the 1986-88 base period. This commitment on support reductions could be applied on commodity grouping rather than on individual commodities.

The level of the domestic support provided for an agricultural product is measured (and monitored) on the basis of the "Aggregate Measurement of Support" (AMS), which is an indicator developed by OECD at an earlier stage<sup>4</sup>. Therefore, the crucial issue for the principal negotiators in this category of commitments was not so much the lower or higher level of reduction, but rather to agree *which forms/measures* of support would be included into the calculation of the AMS for each Contracting Party. In other words, which measures would be subject or not to the reduction commitments and which would be exempted.

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<sup>2</sup> In this respect, each year, the EU Commission calculates the trigger price for each product based on a representative world market price and the cif import price.

<sup>3</sup> See footnote 7.

<sup>4</sup> The AMS was the result of adapting other indicators used by OECD, and in particular, the Producer and Consumer Subsidy Equivalent (PSE, CSE). It was designed to express and compare the various measures of support that affect production and trade. Generally, it is based on the difference between the domestic and world price of each commodity multiplied by the volume of its production.

At the end, the domestic support measures were classified into three lists or “boxes” and agreed:

- The “*Yellow Box*” including all the price supports and aids that definitely affect the size of production and trade and, therefore, been considered as trade-distorting measures, are under the agreed reduction commitment over the 6-year period,
- The “*Green Box*” including all the measures that have *no effect* on trade or production (completely decoupled measures) and are totally exempted from any reduction,
- The “*Blue Box*” including various types of aids that are linked to limiting production schemes. According to this sophisticated definition, the measures included in the “Blue Box” are not clearly defined as supportive measures with no or some effect on production and trade. However, they are also totally exempted from reductions (like the measures included into the “Green Box”) for, at least, the given period of the “Peace Clause”, and they are referred as:
  - The acreage aids granted to crops on the basis of fixed yields
  - The aids that do not exceed 85% of the baseline production level
  - The aids granted to livestock production (premia) on the basis of fixed number of animal units

Clearly, the “Blue Box”, which was originally a basic element of the “Blair House Agreement” between the EU and the US, intends to keep out of any commitment for reduction two specific measures:

- The direct Compensatory Payments (CPs) introduced by in the 1992 CAP reform and applied since then by the EU, and
- The deficiency payments applied by the US in implementing its agricultural policy<sup>5</sup>.

Though agreed, the “Blue Box” arrangement is a controversial and increasingly disputed issue. From the side of the EU, the CPs included into the “Blue Box” are largely production-neutral (since they are based on historical production and do not fluctuate with the level of output) and therefore justified to continue to be exempted from any reduction even in the future. From the side of the US and the CAIRNS, the “Blue Box” category has been inverted as a *transitional* measure in the URAA. It reflected the need to establish a middle ground between the major negotiating parties to address specific problems in their agriculture. The policy measures included, however, should not be considered as decoupled from the production and therefore are not eligible to enjoy the status of the “Green Box” measures.

### **4.3 Export Subsidies**

The most important element of the commitments in this category was the fact that the Agreement tackled not only on the *value* of subsidies but also on the *volume* of subsidized exports. In particular, and on the basis of *1986-90 reference period*, the export subsidies should be reduced over 6 years, by:

- 21% by volume of subsidised exports(with the exemption of processed products) and
- 36% by direct expenditure on export subsidies (ad valorem)

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<sup>5</sup> Under the 1996 Fair Act, the US officially removed all the support measures, and thereof the deficiency payments previously applied, away from production. In so far, and despite the Fair Act, the US has introduced other support measures to the benefit of its farmers (export credits, tax exemptions, direct subsidies, marketing assistance loans, etc) which, even if they could be considered of an “emergency” nature, are not specifically included into any of the above three boxes.

The agricultural exports have been divided into 20 most specific categories (for instance, differentiating wheat and flour from feed grains, or separating cheese, butter and skimmed milk powder from dairy products) in a way that reductions would be made year by year and *by product category*. The exports, however, realised under (permanent or emergent) food aid schemes are exempted from the commitments, on the assumption that are not linked to commercial exports.

#### **4.4. Other Commitments**

From what has been noted before, it is clear that the overall result of the URAA implies *a number of significant changes in (scheduling and applying) the agricultural policies all over the world*. And this is because, it was only after this Round when agriculture was fully integrated into the GATT/WTO system. In fact, after the URAA, agricultural policies and, in particular CAP, *could never be the same in the future* as used to be in the past. In this respect, some other commitments should be also taken into account:

##### **4.4.1. Peace Clause**

Perhaps one of the most important elements included into the URAA (Article 13) is the so-called “**Peace Clause**”, under which, policy measures related to internal support and export subsidies that comply with the Agreement *will not be challenged under the WTO procedures*. Following the Blair House compromise for its 10-year duration, the Peace Clause expires at the end of 2003.

##### **4.4.2. Sanitary and Phytosanitary (SPS) Agreement**

To ensure that technical measures are not used as non-tariff barriers in the future, the signatories agreed to set up a forum for consultations, under the WTO, the “Committee on Sanitary and Phytosanitary Measures”. The main aim of this Committee would be to supplement the existing standards code<sup>6</sup> by further promoting the international harmonisation on these delicate and highly scientific issues. In this process, other specialised multinational Organisations (International Office of Epizootics, International Convention for Plant Protection, Codex Alimentarius) would have to play an important role in establishing the technical standards.

In monitoring the above process, the Committee may approve the use of higher than the agreed standards on the basis of “*scientific evidence*” or as a consequence of “*risk assessment*”. These terms, however, being open also to legal interpretations, have raised already a number of important disputes among the main signatories, in terms, for instance, of using or not the so-called “*precautionary principle*” in taking restrictive measures on trade of agricultural and food products.

##### **4.4.3. Some other specialised issues**

Apart of the above general commitments applied by all the signatories of URAA, the two main actors, the EU and the US, agreed also on the basis of a bilateral compromise (Blair

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<sup>6</sup> The “code” is known as the “Technical Barriers to Trade (TBT) Agreement”

House Agreement) some partial but directly related with the status of CAP concessions on certain sectors (oilseeds, corn, malt, non-food plantings on set-aside land, etc)

## 5. The agricultural agenda of the next Round

Well before the expiration of the URAA in the middle of 2000, a new Round has been announced to start in 30 November 1999, in Seattle, USA.

It is reasonably expected that Agriculture will be again at the centre of the negotiations in the next Round. In addition, it seems that all the Contracting Parties (the EU in particular) are aware of the fact that there will be a strong pressure “to continue the process towards greater liberalisation” in agricultural trade that started in the previous Round. Therefore, it is rather obvious that the overall approach of the future negotiations will be to deal with the issues that remained unresolved by the URAA, since URAA is considered to be only the start towards the liberalisation process. After all, the same actors, as before, have already declared their aims and targets during the next Round.

In relation to the assessments of the URAA and based on the announcements or declarations already made by the principal actors of the game (the US and the Cairns group, the EU and Japan), one could reasonably expect that, in each policy area, the agenda of the future negotiations will include the following issues.

### 5.1. Market Access

- *Tariff rates:* The most important element of the URAA, the “tariffication”, should be considered as a permanent part of the agricultural trade from now on. However, although bound, the tariff levels for agricultural products were set at a high level, outweighing in most cases the average level of the previously applied levies and other non-tariff measures. Therefore, the tariff reductions agreed in URAA have had little effect on the access that the big exporting countries could have to rich consumer markets. It is estimated that agricultural tariffs average above 40% as compared with manufacturing tariffs (which have been almost eliminated or they stand around 5-10% in most industrial countries). In addition, for a number of agricultural products, certain countries still apply even tariff peaks (the so-called “mega-tariffs”) of over 300%<sup>7</sup>. Given that the US and the Cairns Group are united in their aim at further large reductions of tariffs, possibly with maximum tariff rates, it should be expected that, at least, a certain reduction of tariffs on agricultural products would be resulted (above all) out of the next Round.
- *Safeguard Clause:* The Cairns Group has insisted that will raise this issue as no longer necessary and it should be abolished. It is not clear what the position of the US will be, given that it was one of the least signatories that invoked this clause in the recent past<sup>8</sup>.

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<sup>7</sup> T. Josling (see references) chooses as examples of such megatariffs, the cases of Canada (299% on butter and 289% on cheese in 2000) and of India (97% for unprocessed and 139% for processed products)

<sup>8</sup> By invoking the safeguard clause in June 1998, the US imposed quotas on imports of *wheat gluten* from the EU and Australia for a 3-year period. The US asserted that the EU, in particular, realises unfairly subsidising wheat gluten exports and, for this reason, the EU quota was set at a half volume compared to its 1997 exports.

According to the EU regime, however, wheat gluten (commonly used in the baking industry) does not get any export refund. There is only a starch production subsidy (which is supposed

On the other side, Japan is expected to seek to maintain as much of its current border protective mechanisms as possible, while the EU has already declared its aim to maintain or renew this clause against any potential market disturbance by excessive imports.

- *Minimum market access:* It seems that the access arrangements of URAA will form a major target for both the US and the Cairns, which have already declared their objective for a higher than 5% share of the internal consumption. The US, in particular, is likely to aim initially for the elimination of the tariff quotas or at their considerable expansion. Although the EU is expected to fight against this prospect, it seems that it is also ready to make some concessions on this issue, since it has included in its objectives a better access to import markets. However, it is quite probable that the EU will be faced with three types of requests on this issue:
  - An increase of the minimum access in its own rich consumers' internal market at a level much higher than 5% of its internal consumption for each group of products (a result that could be attained by changing also the reference period from 1986-88 to a more representative period of consumption)
  - Elimination of the aggregation (groupings of products) and making minimum access commitment on a product by product basis
  - Inclusion of all the sectors (and not only those subject to tariffication) into the minimum access commitment. (Among other things, such an approach would certainly create great disputes inside the EU, among the M-S, in regards especially to the general treatment of the Mediterranean products)

## 5.2. Domestic Support

- *Base period:* It has been repeatedly remarked that, during the reference period of 1986-88 on which the commitments of URAA were based for the calculation of the AMS indicator, the levels of domestic support were at their peak. Due to this fact, the commitment of the 20% reduction had very little or no impact on the overall level of domestic support. Therefore, the same period could not be considered as a representative one for further commitments. It is rather sure that the future negotiations will make a focus on this point and, perhaps, controversies would inevitably arise as to which period should be chosen.
- *Commodity groupings:* In certain cases, the groupings allowed to make higher support reductions for some less important products and prevented significant reductions in others that are considered much more important in terms of inter-trade. The issue is expected to be raised on the insistence mainly of the Cairns group.
- *The "blue box" issue:* The maintenance or not of the "blue box" will become, quite possibly, one of the major issues during the forthcoming negotiations. The US do not seem to have anymore interest on this, since they (claim that) have turned their previous "deficiency payments" into completely "production-neutral" policy measures. The Cairns have already called for an end to "Blue Box" measures and a redefinition of domestic support, to eliminate all the ambiguities that allow trade-distorting practices. As it has

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to bridge the gap between the price of EU raw materials and the world market price - but this is compatible with the WTO commitments). In retaliation against the decision by the US, the Commission approved in July 1998, an import tariff duty on US *corn gluten*. However, this duty cannot come into effect until June 2001, because, having the US quotas officially described as a "safeguard measure", they are protected from retaliation under WTO for three years.

been mentioned before, the measures included into "Blue Box" are considered as partially decoupled from production but were exempted from reductions on the grounds that they help to curb output. The measures are also exempted from any major ambiguity until 2003, when the "Peace Clause" expires. However, since the EU started replacing the previous price support system into a system of direct support schemes, the CPs become a rather permanent part of CAP and their acceptability in the future trade agreements is increasingly challenging for the world trade partners. Mostly externally but also internally (for budgetary and other reasons), voices have been raised against the (infinite) continuation of CPs, as they stand, implying that, in the future, the "Blue Box" measures should, either be included into the AMS reduction commitments or become subject to a separate reduction commitment. It seems inevitable that the EU system of CPs will come under pressure from both, the US and the Cairns, in the forthcoming Round.

### 5.3. *Export subsidies*

This is the most disputed issue among the main actors and it is reasonably expected that the negotiations will focus on this category of measures in terms of both, the volume of subsidised exports and the overall expenditure dedicated for subsidies.

- The group of Cairns has already declared that their first priority would be the complete elimination of export subsidies.
- The US would favour a substantial reduction of export subsidies, although, despite the rhetorics, it is not clear to what extent, since they have activated or put aside mechanisms that are considered as kinds of export subsidies as well<sup>9</sup>
- The EU seems to be prepared for making further concessions on this issue. After all, the new reform of CAP has been decided on the grounds of decreasing the guaranteed prices at a level (though not sufficient) enabling to shorten the gap between internal and world prices. This would allow also export refunds to be decreased considerably (if not eliminated) in the next 3-4 years. However, the EU's target would be two-fold:
  - To take an offensive stance against US export credits and state trading enterprises
  - To retain the right to utilise export refunds, when necessary

A principal EU *condition*, however, for making further concessions on export subsidies would be to make sure that "blue box" is retained.

## 6. The EU Approach

The EU being quite aware of the forthcoming Round, has already formally adopted (May 1999) a new reform of CAP to be implemented during the period 2000-2006 in the framework of a broader package of measures, the well known Agenda 2000. It is supposed that one of the most important targets of the new CAP reform was to allow the EU to go into

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<sup>9</sup> Export credits and tax exemptions for exporters through "Foreign Sales Corporations" are often mentioned as good examples. In May 1998, the US administration announced measures to reactivate the tools of their "Export Enhancing Programme". The programme is supposed to act as a "safety net". Its aim would be to facilitate exports by adopting a number of export-promoting measures. Such measures included: Subsidisation of the sales of poultry meat in middle East; financial guarantee to exporters selling at regions where import requirements were strict and unpredictable and who would otherwise be reluctant to commit to an export contract; Compensate traders who had to send a shipment onto another destination if it was blocked in the original port on health grounds (example: The Greek authorities prohibited a consignment of US wheat, in May 1998, which was then sold onto FYROM with additional transport costs)

the next Round with more aggressive stance and to leave ground for defending the so called "European model of Agriculture"<sup>10</sup>.

In relation to the new round, the Berlin Agreement on Agenda 2000 (March 1999) included a reference by stating that "the decisions adopted regarding the new CAP reform would constitute essential elements in defining the Commission's negotiating mandate for the future multilateral negotiations at the WTO." Agenda 2000, therefore, forms the *core* of EU's negotiating positions.

In line with this (binding) declaration and shortly after the formal adoption of the reform, in the beginning of last July 1999, the Commission communicated its negotiating priorities and asked for their approval from the EU Council of Ministers and the European Parliament. The Council of Ministers for Agriculture unanimously agreed to back the Commission's agenda on the issue<sup>11</sup>, while the Council of Foreign Ministers is also expected to formally approve the final mandate to the Commission at its meeting of 11/10/1999.

Although there is a clear determination to avoid taking a "defensive" role in the next round, the priorities set by the Commission, as broadly listed, could be still identified as either defensive or/and aggressive:

*"Defensive" issues:*

- A successful defense of the "blue box"
- Renewal of the "Peace Clause" after the year 2003
- Renewal of the "special safeguard provisions"
- Secure that its rural and environmental policies are compatible with the new trade order
- Defense of the "multifunctional" role of agriculture

*"Aggressive" issues:*

- Improved access to third countries' markets
- Intention to target the US' use of export credits and state trading enterprises
- Bring into the negotiating arena new issues, including food safety and quality, trade and environment, animal welfare
- An overall agreement on the Round as a comprehensive "single undertaking"

The EU stance in each one of the above priorities has as follows:

### **6.1. "Blue box"**

Without doubt, the maintenance of the "Blue Box" as one of the existing provisions in the URAA "on which key elements of the EU's agricultural policy is built", will be a priority objective for the EU. In its communication of July 1999, the Commission has clearly pointed out that the defense of the "blue box" is considered "essential to ensure implementation of CAP reform". Additionally, Commission's officials have repeatedly rejected suggestions that

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<sup>10</sup> It is usually mentioned that EU has not clearly defined this model. The Commission has described that the main line of the model should be "diverse forms of agriculture, rich in tradition, which are not just output-oriented but seek to maintain the visual amenity of the European countryside as well as vibrant and active rural communities, generating and maintaining employment". See A. Swinbank (references)

<sup>11</sup> During its informal meeting in Tampere, Finland on 13-14/9/1999, the Council of Ministers for Agriculture outlined a partial "mandate" to the Commission, concerning the agricultural part of the forthcoming negotiations.

the next Round would force the EU into a further set of (substantial) reforms (as it was the case of the previous UR, when the 1992 reform became inevitable before the round was concluded). However, one could raise two points here:

- As a result of watering down the initial proposals of the Commission concerning the price cuts of the most important Common Organisations of Markets, the Berlin agreement (March 1999) on the new CAP reform included the prospect of mid-term reviews of certain policies, at around 2002/2003. These “clauses” indicate that, most probably, the EU will be forced to revise the decisions that have been taken in the light of the agreed financial framework for the whole period, but also of the eastward enlargement. Among other things, since the CPs already absorb more than half of the total EU agricultural budget, their overall size in the near future becomes rather questionable, for internal reasons.
- It is also true that the reform package (and the financial framework agreed thereof) does not go beyond 2006. In this sense, the possibility of some sort of commitment for the future of CPs beyond 2006 (at a time when the round would have been terminated and the EU would have experienced the first wave of new accessions from CEECs) is left open.

Entering into the new round, however, the EU's objective is to preserve the right to maintain CPs either in the current "Blue Box" category or as environmental/social adjustment measures. The Agenda 2000 CAP reform, leave some ground for manipulation:

- The CPs would only partly compensate the loss of income in arable crops, as they will be reduced proportionately in cases when internal average market prices are higher than the intervention prices
- To a certain extent, the CPs have become “greener” through the “cross compliance” scheme, which has been introduced as a measure (though not obligatory for the M-S) making the CPs conditional on environmental requirements
- The CPs will not be provided for the farmers of the CEECs after their accession

Overall, the chances of defending the mechanism of CPs in the new round appear to be half to half. From the one side, since the CPs were introduced in 1992, the Commission has maintained that they are largely production-neutral because they are based on historical production and do not fluctuate with the level of output. In addition, they are fixed and not linked to changes in the world market prices. And it is true that, even if the EU converted a large part of its AMS into direct support schemes, the CPs are paid in such a way that:

- do not create additional incentives to increase the crop area planted or numbers of animals produced;
- do not increase yields by the use of additional variable inputs;
- do not act as a disincentive to consumption.

On the other hand, one should take into account the following parameters:

- OECD has reported that the CPs have replaced market support in the sum total of support (contributing 50-60% in the income of EU's farmers), indicating therefore the market distorting nature of CPs.
- The total amount of CPs to the individual producers is still dependent upon the historic reference yield of each region or upon the number of animals kept and, therefore, they still sustain production.
- Harmonising the CPs for cereals and oilseeds into one arable area payment does not detach them from the area planted
- Reports argue that, even if the CPs are completely detached from production, their continuation beyond a transitional period cannot be justified, unless they are payments for

some legitimate public good provisions (in the form of rural development and cultural landscape)

- It is clear that, whatever EU does with the CPs in the future, even completely decoupled, the international competitors would find arguments to attack them. In fact, it is not the measure as such provocative, but the ability of EU farmers to get a good income allowing them, to a large extent, to stay in the sector and increase their production and export potentialities<sup>12</sup>.

## ***6.2. Peace clause***

The clause exempts the policy measures of CAP (including the CPs) from any WTO challenge up to the time of its expiration, in 2003, provided that these measures are in conformity with the provisions of the URAA. The continuation of the “peace clause” in the future, on the grounds of a new WTO agreement, seems to be vital to EU; it would provide a legal security for the outcome of the negotiations, and this would allow EU to implement its reform in a smooth and comfortable way. In this sense, it looks also imperative for the EU to have a rapid round of negotiations, before the expiry of the current peace clause. Otherwise, if the clause is not rolled-over, all the fundamental mechanisms of CAP (domestic support schemes, export subsidies, etc) could be subject to a succession of hostile Panel reports in the following years. For instance:

- Under the Subsidies Code (GATT Article XXIII), domestic support schemes (including the CPs) could be challenged by countervailing duties,
- Under GATT Article XVI, any kind of the “export subsidisation” component could be also challenged
- Under GATT Article XXIV, any current or future Free Trade Areas agreed and established between EU and other countries (Mediterranean, S. Africa, Mercosur, etc) that could exclude substantial agricultural sectors, will be open to WTO challenge.

## ***6.3. Special Safeguard Clause***

Although the EU has not invoked this clause since the URAA came into force, it is still considered essential to be used as a “safety net” in protecting the EU internal market against a potential surge in imports. This approach is rather in line with the overall intention of EU to continue keeping in the future many of the current essential mechanisms of CAP (intervention purchase, set-aside, export refunds etc) as “safety nets”. In its objective, EU will be joined, most probably, by Japan, which is also expected, on the same line, to seek to maintain as much of its current protective mechanisms as possible. On the other hand, the US's stance is not clear on this issue. The Cairns, however, have already insisted that they will raise the issue of the "special clause" for imports, as no longer necessary and it should be abolished.

## ***6.4. Rural Development and Agri-environmental measures – Multifunctionality of Agriculture***

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<sup>12</sup> The EU having been the first world importer and the second larger exporter of the agricultural and food products, it seems that the overall target of the trade competitors would be to push towards a European agriculture without any preservation, since any kind of preservation could be easily criticised as an "unfair advantage" against the farmers of, at least, the developing countries.

It is clear that the underway new reform of CAP aims inherently to a gradual shift in emphasis of CAP from the support of markets and production to the restructuring of rural areas and rural employment. Even if the new structural measures are considered inadequately funded, the multifunctional role of agriculture in managing the country-side has been carefully raised the last years, under the concept of an *integrated rural development strategy*<sup>13</sup> (in line with the overall objective of “sustainable development”, which has been included in Amsterdam Treaty – June 1997).

Since the protection of agricultural incomes is implied as one of the ultimate objectives of CAP (Article 33.b of consolidated EC Treaty), the definition of “multifunctional agriculture” seeks actually to justify the use of financial support to farming in order to preserve the rural communities and the environment. To this extent, certain types of policy support measures are indispensable. The EU is determined not only to defend this issue in the next round but also to push it as a “non-trade concern” in a future trade agreement. The justification would be that “multifunctionality” covers not only the production of goods and raw materials but also public goods, as preserving the countryside heritage, environmental benefits, leisure, etc. However, the food exporting countries regard the issue of “multifunctionality” with suspicion rather, looking in it a potential excuse for continuing to treat agricultural products as special cases in terms of trade rules.

The EU, although in ally with Japan on this issue, expects that, apart of the CPs, all measures included under the structural, rural or agri-environmental policy will be scrutinised for their compatibility with the “green box” criteria. If found faulty, the EU would have to adopt other, more decoupled alternatives. For instance, the “Less Favoured Areas” scheme that provides for special assistance aids to farmers engaged in certain EU agricultural areas, has changed under the new reform by gradually transforming the aids from a production to a per hectare basis. Even so, however, it is not quite sure whether the new arrangement meets the requirements for a complete decoupling from the production.

Direct aid measures, however, even with minimal trade impact, are considered indispensable. For this reason, the EU supports the idea of *making the “green box” criteria more flexible*, even if the trade partners have rather expressed the opposite objective; to review and make the “green” criteria more tightened.

### ***6.5. Improved access to third markets***

The EU expects that after the full implementation of the new CAP reform and on the assumption that world prices will remain at reasonably high level, the existing gap between the domestic and world prices will decrease considerably or even eliminated. Therefore, under normal circumstances, the export subsidies for a number of products would not be necessary. Taking into account the prospects of expanding world demand on food products, the EU aims at taking full advantage of the new opportunities that would appear in the near future. In this respect, the EU is rather prepared to make concessions related to its own market on the assumption that certain barriers to market access of third countries (including tariff quotas) are also lifted.

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<sup>13</sup> This concept was formally introduced by the EU in November 1996, when an important Conference took place in Cork, Ireland, under the auspices of the Commission, the outcome of which was the well-known “Cork Declaration”.

## **6.6. USA's subsidies**

In the new Round, the EU has clarified its intention to look rather hard at the support schemes of its trade partners<sup>14</sup>. To counterbalance any attack on CPs included into the "blue box", the EU argues that many other countries have made use of support payments under the same box.

By taking an offensive stance against the US export credits in particular, the EU argues that export subsidies are not just about refunds but also all kinds of support that function as export subsidies and have to be tackled during the next round<sup>15</sup>. For the time being and under the URAA, refunds are subject to limitations already, but export credits (as well as food aid been available under credit terms) remain mostly under no WTO discipline and should be subject to compliance with agreed trade rules. The issue has been pointed out even by OECD that has noted an increasing tendency to use export credits to support a wider area of trade (especially since the emergence of the economic crises in Asia and Russia). The same applies for the State Trading Corporations, which in certain cases act as state monopolies in the world trade.

## **6.7. Non-trade concerns**

To the EU's view, Article 20 of the Marrakesh Agreement provides that negotiations on key trade issues can also cover non-trade related matters. It is sure that, apart of the "multifunctionality" mentioned above, the EU will put high on the list of its objectives some other issues of non-trade concerns of particular importance:

### **6.7.1. Agricultural environment**

The intention for the negotiations is to cover potential environmental threats arising from agricultural trade liberalisation and push towards accepting the so-called "eco-conditionality" principle in scheduling and applying the agricultural policies. During the last years this issue attracts more and more the attention not only of environment activists but also of independent researchers and experts<sup>16</sup>. To the EU's understanding, farmers exercising environment-friendly practices should be able to be compensated for offering additional services to the public.

### **6.7.2. Food safety and quality**

The EU wishes to ensure that greater attention is paid to the justified interests of consumers and that the WTO is not used as a pretext that allows placing products on the market "where there are legitimate concerns about their safety", according to the Commission's view. This

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<sup>14</sup> The E. Commission has recently promised that will set up a special unit in DG VI to examine claims about the WTO compatibility of the US Farm Bill in anticipation of the next round. The Unit will examine in particular whether the Fair Act payments are really decoupled, as they might be given in a way that farmers do not have absolute choice which crops to plant. A range of other areas will be also looked where the US might be found to be paying hidden subsidies to farmers.

<sup>15</sup> As an example, the US Administration offered recently tax exemptions for exporters through the so-called "Foreign Sales Corporations (FSCs)" which are subsidiaries of US exporting firms based in tax haven countries (Barbados, etc). The FSCs gain income tax relief as long as the product is predominantly produced in the USA. In return, payments from FSCs to their parent companies in the USA are also exempted from tax. To the Commission's view, those tax exemptions constitute trade distorting subsidies "by granting an unfair advantage to US products". (See, also, footnote 7)

<sup>16</sup> A. Layard (see references) interestingly links the trade and environment debate with other important disputes in relation to food safety and animal welfare issues .

reference points out the fundamental difference of interpretation of the sanitary and phytosanitary provisions of the URA, as well as on the "philosophy" of food quality. In particular, the EU aims to maintain the right of applying own scientific assessment standards and, if necessary, to restrict imports on health and consumer grounds. In other words, the EU is determined to clarify and strengthen the existing WTO framework for the use of the "precautionary principle" in the area of food safety (animal and human health protection). A number of disputes still in progress, indicates that the following issues will strain relationships, especially between the main protagonists, EU and USA, in the run up of the next round:

- The growth promoting hormones in beef production<sup>17</sup>
- The genetically modified crop seeds (GMOs) entering into the food chain<sup>18</sup>
- The use of antibiotics as additives in animal feed

After all, the *BSE crisis* and the recent *dioxin* scandal in Belgium would inevitably lead to increasing calls for tighter controls and monitoring in the feed sector, at least across the EU, which would have an increasing link with the trade rules.

### 6.7.3. *Animal welfare*

The animal welfare issue has become already one of the fundamental points of the negotiation mandate for the round. Measures taken already by the EU to raise animal welfare on a rather "ethical" basis, have as a minimum consequence that EU producers should be given protection from imports of similar products, under less-welfare-friendly systems elsewhere. Up to now, three possible approaches are examined:

- A multilateral agreement establishing international welfare standards, and this is the preferred option by the EU)
- The potentiality to impose trade measures against countries whose standards fell short of those required by the importing country
- Labeling of livestock products, as regards the treatment of animals from which the products derive from, to allow consumers' choice<sup>19</sup>

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<sup>17</sup> Growth promoting hormones have been banned in the EU since 1988 on the grounds that they may increase the risk of cancer in humans. Since then, the EU prohibited the imports of hormones-treated beef. In Jan. 1998 a WTO panel on the issue accepted that the 10-year old EU's ban breaks the international trade rules, because it has failed to carry out a full scientific assessment into the alleged risks from hormone use. To comply with the WTO rules, a deadline was set up to 13/05/1999 for the EU to justify the ban on the grounds of the SPS agreement. The EU maintains that the initial scientific studies have provided enough evidence showing the potential risks to consumer health and therefore its ban is justified under the *precautionary principle*. However, the completed scientific research analysis has not been fully carried out yet by the Commission's machinery. Even so, the EU believes that the apparent conflict between consumer health concerns and trade rules has been resolved. The appellate body in the hormones dispute had ruled that "countries had a wide level of discretion to decide their own level of protection". This point of view, however, is not shared by the US and other trade partners. As a result, the US and Canada took retaliatory measures, in effect from 29/07/1999, against imports of certain EU products.

<sup>18</sup> In so long, the issue of biotechnology has not been discussed in the framework of SPS agreement as part of UR settlement. Some Contracting Parties and, in particular, the US, would rather prefer to avoid re-opening the debate over the SPS provisions. However, apart the SPS, other WTO agreements (TBT, Rules of origin, GATT) might prove to have relevance for biotechnology

<sup>19</sup> In particular, compulsory *beef labeling* is supposed to be in place within the EU by Jan. 2000.

Finally, potential other subjects to be raised by EU would be the trade-marking system (the EU's policy on protected designations of origin), and agricultural labour protection.

### ***6.8. Overall agreement of the new round***

It is rather sure that the EU will inevitably have to make concessions on agriculture and should therefore trade off potential losses against gains in other sectors, for instance, financial services. That is why EU favours an overall agreement and not a sector-by-sector approach. In any case, the EU maintains that, like in the previous UR, this new round must be also comprehensive and cover other sectors than agriculture alone.

## **7. Concluding comments**

Many spectators believe that, concerning agricultural trade, only modest progress is likely to be made in the forthcoming Round. It is argued that, in the three main areas of agricultural policies applied by the WTO trade partners (market access, domestic support, export subsidies), it would be a matter of building on what was achieved in the URAA, rather than the introduction of any new radical elements.

If this will be the case, the EU, opposite to the previous UR, will enter the negotiations well prepared this time, by having taken already its decisions towards a new reform of the CAP, which would constitute a given basis (core) for the negotiations. However, even if no radical changes are expected to be agreed, the question arises whether the decisions adopted on CAP will prove to be adequate to meet with even moderate requirements of the new trade obligations.

In this respect, the Berlin Agreement of EU leaders on the new reform of CAP has been criticised, internally and externally, as leaving very little ground for considerable concessions in the trade negotiations. In particular, by making the full implementation of the reform longer and by adopting price cuts for the most important products at a lower rate than initially proposed by the Commission, the EU will be obliged to keep a rather more defensive than offensive stance in the negotiations. For instance, the price cuts will prove to be rather inadequate to eliminate or decrease considerably the use of export subsidies<sup>20</sup>, although it is well known that this issue stands at the top of its trade partners' priorities. The US and the Cairns have already commented that if the EU continued to use these measures, most probably it would form a "major block in the continuum towards trade liberalisation". Some other issues also of the reform package are expected to create more difficulties for the EU. The increase of CPs to the farmers without any form of gradual "degressivity" or "capping" gives the impression that EU aims to keep this form of income support schemes for ever, and this is not going to be easily accepted by the other big trade partners. Then, the new reform is referred only to the most important but limited number of product markets. This is going to be also a challenge for the other parties during the negotiations. The Cairns group, for instance, have pointed out that a number of products of their special interest, like sugar, rice,

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<sup>20</sup> Among other things, the effectiveness or not of the price cuts in eliminating EU export subsidies will depend to a large extent on macroeconomic conditions such as the exchange rate of the euro against the US dollar. A strong euro would decrease the world price for agricultural products in European terms and thus widen the gap between EU prices and the world level, forcing the continued use of export subsidies.

sheep meat, dried fodder, tobacco, olive oil, fruits & vegetables, have remained out of the Agenda 2000 package and should be priority targets for further reform initiatives.

In this respect, the Commission has pointed that the EU will be going into the talks with an “open” perspective. To a certain extent, this would mean that a further reform of CAP will become inevitable before the expiration of Agenda 2000 perspective (2006), as a result not only of meeting other internal needs of EU but mostly as a requirement to meet the new world trade obligations.

As regards the liberalisation process, there is no doubt that agriculture will be again at the centre of the round. But, this time, according to the EU’s approach at least, the food safety issues (sanitary and phyto-sanitary standards), together with the state trading are likely to have a larger importance than in UR. Even if such regulatory issues as the hormones in beef, the GMOs, the labeling requirements, in connection with the BSE crisis, the use of antibiotics in animal feed, etc are not entirely new, their importance seems to be now of high priority.

Once again, the three known protagonists in the agricultural negotiations (the EU, the US and the Cairns group) have firmly deployed their strategy and their arguments. The scene, therefore, is set for a heated and difficult round, which could struggle to meet the 3-year deadline.

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