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World Trade Organization and the Commodity Title of the next Farm Bill

By Doug O'Brien

Attorneys who represent farmers, and especially those who represent producers who receive payments through the Farm Bill, know what an impact that piece of federal legislation has on producers' business decisions. So the Farm Bill can determine a producer's decisions. But what determines the contents of a Farm Bill?

Traditionally, the major factors included the state of the farm economy, the condition of the federal budget, and who is in power in Congress at the time of the bill's consideration. To be sure, all of these factors will again play a major role in the next Farm Bill. But an influence that has many times provided background context to Farm Bill deliberations is now up front and squarely facing policy makers: current and future trade policy. The impact of the Brazil cotton case has shifted current trade policy in a way that may force domestic policy to change. Further, the debate surrounding the next Farm Bill could very well coincide with the negotiations for the next major multi-lateral agricultural trade agreement, known as the World Trade Organization Doha Round. The timing both highlights and heightens the new significance that United States' trade obligations have on domestic policy.

This article examines how this new factor might influence Congress' Farm Bill debate. But first, the article sets the stage by focusing on particular provisions of the 2002 Farm Bill, and examining the World Trade Organization and the U.S.'s obligations under it. This article is designed for the practitioner who works in the agricultural sector and thus discusses the policy changes that may come about in the next few years.

Current policy

2002 Farm Bill commodity programs

This section of the paper examines the three major commodity payment mechanisms in the current farm bill: direct payments, marketing loans, and counter cyclical payments.[1] Before discussing those individual mechanisms, the paper will first look at some general rules of eligibility and limitations, all of which are important in the context of U.S. trade obligations.[2]

The statute requires the Secretary to make payments to producers, who are individually defined as "an owner, operator, landlord, tenant, or sharecropper that shares in the risk of producing a crop and is entitled to share in the crop available for marketing from the farm."[3] The regulations require that the person be "actively engaged in farming," a phrase to which the Code of Federal Regulations devotes an entire subpart.[4] In general, to be actively engaged in farming a person must make significant contributions of both (1) capital, land and/or equipment, and (2) personal labor and/or management.[5] Recipients of commodity payments must also agree to relatively minimal conservation requirements,[6] as opposed to pre-1996 when farmers might be required to remove up to fifteen percent of their cropland from production. The current "highly erodible land" requirements simply oblige farmers to exercise certain conservation practices that limit soil erosion on highly erodible land and generally prohibit the conversion of previously uncultivated land and wetlands[7] (programs popularly known as sodbuster and swampbuster, respectively).

The major limiting factors for producers are the number of acres one is allowed to enroll, the number of bushels covered and the total amount of money one may receive under the different programs. In general, the number of acres eligible for payment, or "base acres", is not based on the actual number of acres planted for the year that the farmer receives a payment. Rather, base acres is generally the average number of acres planted to covered commodities in the past, for instance from 1998 to 2001,

Cont. on page 2

Doug O'Brien is Senior Staff Attorney at the University of Arkansas School of Law, National Agricultural Law Center and at Drake University School of Law, Agricultural Law Center.

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IN FUTURE ISSUES

- The area of potential effect under regulations promulgated by the American Council for Historic Preservation

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- 2005 Conference President-elect Steve Halbrook is well into the planning of an excellent program for the 2006 Annual Agricultural Law Symposium at the Hyatt Regency on the Savannah riverfront in Savannah, Georgia, October 13-14, 2006. As soon as the program is virtually complete, we will post it on the AALA web site. Mark your calendars and plan a trip to "America's First City." Brochures will be printed and mailed as soon as the program plans are complete.

or if the producer prefers, base acres used by the 1996 Farm Bill, which in turn were also based on historical acreage.[8] The result is that one of the major variables in two of the payments, direct payments and counter cyclical payments, could be based on production decisions the farmer made many years prior to the payment. As will be seen, another major variable in the determination of direct payments and counter cyclical payments is the program yield. As with the base acres, the program yield is also based on historical numbers and will not change with the current yield.[9]

Another important limitation is the one that has become the most controversial: the amount of payments a producer may receive under the different types of payment mechanisms. In general, a producer is limited to the following amounts for each program: $40,000 in direct payments; $65,000 in counter cyclical payments; and $75,000 in loan deficiency payments and market loan gains.[10] Well-worn legal devices such as the three-entity rule allow farmers to essentially double the payment limits, and the use of commodity certificates can take the lid off the marketing loan limits.[11]

One other limitation especially important in the eyes of the World Trade Organization is the flexibility provided to producer planting decisions. The 1996 and 2002 Farm Bills provided greater flexibility to producers in whether and what to plant without affecting certain payments. Yet farmers are not completely free to plant what they want. In general, producers seeking subsidies for "covered commodities"[12] may not plant fruits or vegetables on base acres.[13]

The next section will look at the three primary payment mechanisms received by producers of covered commodities.

Direct payments. Producers receive direct payments based exclusively on their base acres and program yield.[14] The direct payments are a remnant of the 1996 Farm Bill Production Flexibility Contract that were to phase out in 2002 but Congress decided to extend. These direct payments are generally decoupled, or unrelated, to current production or price. To arrive at a producer's direct payment, one simply needs to multiply the following three variables by .85: base acres, program yield, and payment rate. The payment rate is the rate provided for in statute.[15]

Counter cyclical payments. Counter cyclical payments signified the return of deficiency payments, which were used in Farm Bills before 1996. Counter cyclical payments are designed to provide a safety net for farmers when prices are low and thus are not paid when prices are high. The countercyclical payment makes up the difference between the target price, which is fixed in statute,[16] and the amount the farmer could have received for producing the crop—including money received when he or she sold the crop, the direct payment, and any marketing loan gain. While the CCP is partially based on the season's actual prices, it is not based on the season's actual production. Like the direct payments, the CCP also uses historical base acres and program yield as variables instead of actual production to determine how many units are eligible for the CCP.

Thus producers could receive CCP payments even if they choose not to plant anything; that is, none of the variables are dependant on actual production. Nevertheless, CCP does have a countercyclical affect because the payment is partially dependant on market prices.

Nonrecourse marketing assistance loans. Nonrecourse loans were a component of both pre-1996 Farm Bills and the 1996 Farm Bill. Marketing loans in theory provide farmers interim financing from the time that the crop is harvested until they decide to market the crop. The loans were originally designed to give producers the ability to hold on to the crop until the harvest seasonal lows passed. Nonrecourse loans work by allowing farmers to borrow money using the crop as collateral valued at the loan rate, for instance $1.95 per bushel of corn.[17] If the actual price falls below the loan rate, the farmer technically has the option of forfeiting the crop, and because the loan is nonrecourse, the farmer does not have to pay the difference between the loan rate and the value of the crop when forfeited. Because there is no recourse for forfeiting a lower-valued crop, the real effect of nonrecourse loans is to set a price floor because a producer will always be able to receive at least the loan rate for his or her crop.

For example, if a farmer borrows money using 10,000 bushel of corn for collateral and the loan rate is $1.95 per bushel, the farmer receives a loan of $19,500. If at a particular time the farmer decides to forfeit the corn, although it is worth only $1.70 per bushel or $17,000 total at the time of forfeiture, he will be free of his loan obligation because the loan is nonrecourse. The farmer enjoys a loan gain of $.25 per bushel or $2500. The real result is that the farmer was able to receive $1.95 per bushel of corn even though the market price was only $1.70.

To avoid massive forfeitures and direct commodities on to the market, Congress has provided producers alternatives for

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AALA Editor..........................Linda Grim McCormick

2816 C.R. 163, Alvin, TX 77511
Phone: (281) 388-0155
E-mail: apamperedchef@ev1.net

Contributing Editors: Doug O'Brien, University of Arkansas, Fayetteville, AR.

For AALA membership information, contact Robert Achenbach, Interim Executive Director, AALA, P.O. Box 2025, Eugene, OR 97405. Phone 541-485-1090. E-mail RobertA@aglaw-assn.org.

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June 27, 2006 — St. Louis, MO — Sixth International Biotechnology Roundtable

John Danforth Plant Science Center, St. Louis, Missouri, 8:30 AM. to 6:30 PM

Sponsored by the Section On Environment, Energy & Resources in cooperation with the Council For Agricultural Science & Technology and the American Agricultural Law Society.

The program will discuss such questions as: Will the Biosafety Protocol create barriers to commercial markets for innovation from public research? Will export commodities shipments require specific identification of all "genetic events" present in any biotech crops that they "may contain" (under BSP Article 18.2(a) - if so, will this lead to trade barriers to corn, soy, cotton, canola shipments containing traces of biotech crops ("genetic transformation events") that lack regulatory approval in one or more overseas markets? What should the Biosafety Protocol parties consider in passing national or multilateral regulation and liability regimes to implement elements of the Biosafety Protocol? How will U.S. and other exporting nations react to the "economic loss" threatened by the Protocol? What are the liability standards for recovering economic loss arising from trade disruption or barriers to trade? *Contact:* Thomas Redick (866) 444-7529 for registration information or speaker details. thomasredick@netscape.net

receiving the loan gain. Instead of forfeiting the commodity, the producers may choose simply to pay off the loan at the lower market price,[18] thus receiving the advantage of the difference between the loan rate and the market price. The statute limits the amount a producer may receive on these marketing loan gains to $75,000 per person. On a variation of this marketing loan gain, producers can in effect take part in a paper shuffle that allows them to pay back the loan with commodity certificates. The economic benefit is the same for the producer; the only major difference is that gains received when using commodity certificates are not limited. Finally, farmers can avoid putting their crop under loan altogether and still receive an equivalent to the marketing loan gain called a loan deficiency payment, which are subject to the $75,000 payment limit.[19]

The key for this article's purpose is that producers receive these type of benefits based on actual production.

World Trade Organization

As stated on its website, "the World Trade Organization (WTO) is the only international organization dealing with the global rules of trade between nations."[20] The organization was created in 1994 and as of December 2005 included 149 countries as members. The main functions of the WTO are to serve as a forum for trade negotiations, administer WTO trade agreements and handle trade disputes.[21] Beyond the general agreements establishing the WTO and setting the rules of dispute resolution, the main WTO agreements are those covering the general areas of goods, services, and intellectual property.[22] Under these umbrella agreements are more specific agreements, such as the Agreement on Agriculture that falls under the umbrella agreement on goods known as the General Agreement on Tariffs and Trade (GATT). Appended to the Agreement on Agriculture is each country's Schedule of Concessions that lists specific country commitments.

The Agreement on Agriculture was one of the major results of the Uruguay Round of negotiations, which took place from 1988 to 1994. The Agreement is by far the most significant international trade agreement affecting agriculture, a sector known for its protected status throughout history. Although its precise impact thus far is difficult to gauge, the major significance of the Agreement on Agriculture is simply the creation of mechanisms to regulate agricultural trade.[23]

The Agreement on Agriculture addresses three subjects: market access, domestic support, and export subsidies.[24] On market access, the Agreement on Agriculture required countries to undergo tarrification,[25] which means the conversion of non-tariff trade restrictions such as quotas to tariffs. For example, if a country has a quota restricting the amount of kumquats that it will allow into the country, the agreement requires that the quota be converted into a tariff that would result in the same number of imported kumquats. Although the immediate result is the same as quotas, tarrification provides for greater transparency which makes it easier to reduce tariffs. The Agreement on Agriculture also requires a gradual reduction of tariffs over time.

Domestic support refers to subsidies provided to agricultural producers.[26] The Agreement on Agriculture divides the types of support into different categories determined by whether the support has an effect on agricultural production. The categories are known as amber box, blue box, and green box.

Subsidies included in the amber box are those deemed to have trade-distorting effects or that affect production. Amber box subsidies are limited under the Agreement on Agriculture as calculated under the Aggregate Measure of Support (AMS).[27] The Agreement on Agriculture requires countries to reduce the AMS by a certain percentage, depending on whether the country is developed or developing. For developed countries, the AMS was reduced by twenty percent, while developing countries reduced their AMS by thirteen percent. The main examples of amber box subsidies in U.S. policy are the marketing loan benefits, including loan deficiency payments and marketing loan gains.[28]

Subsidies included in the blue box cover production-distorting subsidies that require farmers to limit production.[29] These types of subsidies are used very rarely in the United States, and at any rate are not included in the AMS. A historical example of this type of subsidy is the target price deficiency payments that were a feature of pre-1996 Farm Bills and that required farmers to idle part of their productive land in return for the right to obtain deficiency payments.

Domestic supports categorized in the green box are deemed not to distort trade and thus are not included in the AMS. Support falling under this category includes funding for agricultural research, conservation, rural development, domestic food aid and disaster payments.[30] The U.S. has argued that direct payments under the 2002 Farm Bill should be included in the green box, but the WTO Cotton case discussed below ruled that direct payments cannot be categorized in the green box and thus were included in the amber box for the Peace Clause determination.[31]

Beyond the exemptions provided in the green and blue boxes, the Agreement on Agriculture also provides two types of de minimus exceptions to the AMS.[32] Product-specific domestic support focuses on the different types of amber box supports used for a particular product and exempts these supports if the total value does not exceed five percent of the total value of production of that product. Non-product-specific support is exempt if all amber box support used in the country for all products is less then five percent of the total value of production of all products in the country.

In the Agreement on Agriculture the U.S. is committed to limiting its AMS to $19.1 billion per year. When trying to determine whether a program is included in the AMS, one analyst provides this helpful list of questions:[33]

1. Can the program be categorized within the green box, i.e., does not distort trade?

2. Can the program be classified under the blue box, i.e., a production-limiting program?

3. Does the support fall within either the product-specific or non-product-specific de minimus exceptions?

If the answer to any of these questions is yes, then a country is not required to include the program expenditures in the AMS. Otherwise, the domestic support should be added to AMS.

Export Subsidies. "Export subsidies are special incentives in the form of direct or indirect compensation provided by governments to commercial firms to encourage increased foreign sales of domestic products."[34] Examples of export subsidies include direct export payments to exporting firms and gifts or sales of government stocks below the market price.[35] The Agreement on Agriculture requires developed countries to reduce the value of subsidized exports by 36 percent over six years (1995-2001).[36] While direct export subsidies are subject to these commitments, indirect subsidies such as credit guarantees are subject to some debate.

Agreement on Subsidies and Countervailing Measures. The Agreement on Subsidies and Countervailing Measures (SCM) is the agreement that generally provides disciplines on subsidies and limits what countries can do to counter others' subsidies.[37] Discussed below, the Peace Clause in the Agreement on Agriculture largely exempted agriculture from provisions of the SCM Agreement.[38] With the Peace Clause's expiration in 2004, however, the SCM now generally applies to agriculture.

The SCM divides its treatment of subsidies into more general "actionable subsidies"[39] and more precise "prohibited subsidies." Prohibited subsidies include subsides contingent on export performance (export subsidies) and subsidies contingent on the use of domestic over imported goods.[40] Export subsidies for agricultural goods are not subject to this prohibition, but are rather limited by the Agreement on Agriculture.[41] "Actionable subsidies are countervailable, if they cause mate-

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Farm Bill/Cont. from page 3
rial injury to domestic industry. In addition, actionable subsidies (for example, government benefits to a specific enterprise or industry), even if not prohibited, nonetheless may be subject to challenge under the agreement if used in a way so as to cause 'serious prejudice' to the interests of another WTO member."[42] Serious prejudice may arise when "the effect of the subsidy is to displace" imports, undercut prices of competing products, or increase the world market share of the particular product.[43] One commentator summarizes the effect of the SCM in this way: "[W]henever a government confers a financial benefit to a specific group of producers, such benefit will amount to a subsidy that may be challenged by another WTO member if that subsidy caused 'serous prejudice' to its interests."[44]

Peace Clause in the Agreement on Agriculture. The Agreement on Agricultural protected countries from some claims that otherwise would have been actionable under the SCM.[45] What is popularly known as the Peace Clause expired in January of 2004.[46] Before it expired, the clause suspended the application of the Agreement on SCM to most agricultural subsidies, including (1) domestic support that did not violate the limits within the Agreement on Agriculture as long as the support granted to that subsidy was not greater than that provided in 1992,[47] (2) domestic subsidies that fit within the green box,[48] and (3) export subsidies that do not violate the Agreement on Agriculture.[49]

The Dispute settlement process. In any agreement the ultimate question must be: Why would the parties choose to comply? For the United States, there are any number of "soft" reasons generally based on the idea that free trade is a good thing, the U.S. must be a leader in free trade, and if the U.S. flaunts the primary trade agreement it will threaten both the free trade movement and the U.S. position as a trade leader. Beyond this geo-political reasoning, the WTO also provides some hard backstops to enforce its agreements.

Annex 2 to the General Agreement on Tariffs and Trade, the Dispute Settlement Understanding, sets out the rules of handling disputes that come under the Agreement on Agriculture.[50] In general, the DSU encourages members to negotiate trade differences in "consultations."[51] These consultations could be compared to mandatory mediation before a party in a U.S. civil proceeding is able to proceed to litigation. If the consultation does not solve the trade dispute, the parties have the opportunity to establish a panel to hear the dispute.[52] According to the DSU, the panel should hear the case and file a report within six months of convening. Aggrieved parties may appeal the findings of the panel to an appellate body.[53]

The panel report, or in the case of an appeal the appellate report, will include recommendations and rulings of what the violating party should do to come into compliance. Once the panel or appellate report is final, the parties once again have the opportunity to negotiate terms with respect to the adopted recommendations, including compensation for the complaining member. If the parties fail to agree on how to proceed, then the aggrieved party may request the Dispute Settlement Body to suspend certain provisions of WTO agreements that either restrict trade for the aggrieved party or generally help the party that was found to violate the agreement.[54] In short, the process first recommends that a member change their domestic policy to come into compliance, and if it does not do so, the WTO may take away certain rights or impose obligations such as allowing the aggrieved country to impose higher tariffs on the violating party's goods.

Brazilian cotton case

Brazil's complaint against the U.S. cotton program provides an example of the dispute settlement process. A dispute that Brazil initiated in late 2002 went through the consultation and panel process and was appealed by the U.S. In March 2005, the appellate body upheld the panel's finding that portions of the U.S. cotton program violated the Agreement on Agriculture.[55] The most concrete finding was that the U.S. Step 2 program violated the Agreement on Agriculture because the payments were based on export performance. "Step 2 requires the USDA to issue cotton user marketing certificates or cash payments, under certain circumstances, to domestic users (such as textile mills) and exporters of cotton. The Step 2 certificates help to bridge part of the gap between the price of U.S. and foreign growths by 'buying down' part of the difference between the U.S. price and the world price."[56] The Agreement on Subsidies and Countervailing Measures generally prohibits subsidies that are based on export performance or that are contingent upon the use of domestic over foreign supplies.[57] The panel and Appellate Body also found that most of the U.S.'s export credit guarantees are effectively export subsidies not consistent with the U.S.'s WTO obligations. This finding went beyond cotton to include other commodities that participate in the export credit guarantee programs.[58] In response to the WTO decision, Congress repealed the Step 2 program effective on August 1, 2006.[59]

Although cotton was the only commodity involved in the dispute, the WTO decision could have broader impacts because of a preliminary finding having to do with the Peace Clause. Before Brazil could get to the Step 2 claim, it first needed to get over the Peace Clause, which limited a member's ability to challenge a subsidy when the subsidy is below the amount of support for that particular commodity in 1992.[60] To determine the level of support for this Peace Clause question, Brazil argued that direct payments should be included, in opposition to the U.S.'s characterization of direct payments as completely decoupled and thus exempt from the support calculation. Significantly, the panel and appellate body found that direct payments are not completely decoupled because they were partly contingent on producers not planting fruits and vegetables.

Although the Peace Clause no longer applies because it lapsed after the initiation of the Cotton Case, the findings that direct payments are not decoupled may still have weight. This characterization of direct payments as outside the green box has some U.S. policy makers concerned that these payments may subject the U.S. to more WTO challenges in the future. Others, however, point out that the consequences may be limited to the particular case as evaluated strictly in terms of the Peace Clause violation.[61] One stated that "[t]he panel did not specifically reclassify U.S. [direct payments] as 'amber box,' nor did the panel recommend that the United States should notify such future payments as 'amber box.'"[62] At any rate, the finding focusing on the fruit and vegetable limitation does provide a new wrinkle in the Farm Bill debate and at the very least will force Congress to consider the wisdom of continuing that limitation.

The Doha Development Round

Article 20 of the Agreement on Agriculture required that the members begin renegotiating the agricultural provisions in 2000.[63] To formally kick off negotiations, member countries agreed to a ministerial declaration in Doha, Qatar in November 2001.[64] This round of negotiations has become known as the Doha Development round in recognition of the importance of the effect that the eventual agreement will have on developing nations. Peppered throughout the declaration are references to developing and least developed nations that could be summed up in this statement in the second paragraph of the declaration: "[W]e shall continue to make positive efforts designed to ensure that developing countries, and especially the least-developed among them, secure a share in the growth of world trade commensurate with the needs of their economic development."[65] Further evidence of the importance of developing countries is the unprecedented active participation of these countries in the negotiations. A group of member countries known as the G-20 and led by Brazil, India and China has emerged as a major player in the negotiations.[66]

Originally, the Doha Declaration set January 1, 2005 for the completion of negotiations.[67] With agricultural presenting the main snag, the latest schedule agreed to in Hong Kong in December 2005 proposes a new goal of completing negotiations by the end of 2006, with member countries establishing modalities by April 30, 2006.[68] Modalities are the actual mechanisms that will be used by countries to reduce trade distorting policies. For instance, in the Agreement on Agriculture the use of tarrification and the corresponding reduction in tariff rates are modalities.[69]

As of the writing of this article in mid-April, the conventional wisdom is that members will not meet the April 30 deadline. Further, the departure of Rob Portman from the post of U.S. Trade Representative to the Director of the Office of Management and Budget on April 18 has caused many to speculate that the Doha Round may not be completed at all.

Trade promotion authority

Trade Promotion Authority (formerly known as Fast Track negotiating authority, now known as TPA) provides the President the ability to present negotiated trade agreements to Congress for its approval on an up or down vote.[70] Without this authority, Congress has the ability to amend the agreements when they are considered. Such amendments would likely cause a multi-lateral trade agreement to completely unravel. Thus, many observers see the availability of TPA as a key ingredient to U.S.'s involvement in the Doha round. A major complicating factor is that TPA will terminate in July 1, of 2007.[71]

How trade policy will affect future farm policy

The paper thus far has discussed the most significant current domestic and trade policy affecting agriculture. The rest of the paper will look at how these different strains of policy may interact in the near future with an eye toward the rural attorney's obligation to counsel their clients.

Timing of the next Farm Bill and completion of the Doha Round

A perfect storm may be brewing for United States farm policy in the next year: (1) The 2002 Farm Bill will expire at the end of the 2007 growing season, (2) the President's Trade Promotion Authority is set to expire in July 2007, and (3) the Doha round of WTO negotiations is scheduled to be completed in 2006. In reality, the Doha Round may extend beyond the end of 2006, but many question whether it will matter once TPA expires,[72] thus pressure is exerted on members of the WTO to come to an agreement in late 2006 or early 2007. On the domestic front, this means that Congress needs to determine whether to move forward with the drafting of the next Farm Bill or whether to extend the 2002 Bill and rewrite it after the Doha Round is either completed or completely failed.

The Administration has made clear that it wants to move forward with the drafting of the Farm Bill notwithstanding what occurs with the Doha negotiations. Secretary of Agriculture Johanns made clear in early March that he strongly opposes any extension of the 2002 Farm Bill.[73] Meanwhile many of the commodity groups and general farm organizations that have been relatively happy with the 2002 Farm Bill seek to extend its provisions into at least 2008.[74]

U.S. policy makers may see another factor that could determine the timing of the next Farm Bill: additional WTO challenges. The Brazil cotton decision highlighted some of the vulnerabilities of U.S. commodity programs beyond just the cotton program. The status of the direct payments was put in question when the WTO ruled that they could not be categorized as green box payments; thus those payments would likely be categorized within the amber box. Meanwhile many question how countercyclical payments would be categorized if they were challenged. Given that the payments are based on market prices, it is likely that the counter cyclical payments would be categorized under the amber box. One organization in particular raised the specter of WTO challenges in the corn, cotton and rice programs.[75]

Depending on the level of threat of these possible challenges, policy makers have the following choices: (1) essentially maintain the status quo in terms of WTO obligations and the Farm Bill, and thus face the possible consequences of successful WTO challenges; (2) ensure that the Doha Round results in an agreement that allows for current Farm Bill policy, for instance ensuring that countercyclical payments are somehow exempted from the Aggregate Measure of Support, or (3) change the Farm Bill programs to come into line with WTO obligations. The next section considers what Congress might do in the next farm bill in light of these considerations.

Provisions of the new Farm Bill

This section considers some possible policy options for the next Farm Bill in light of trade developments. The logical place to start is to consider current commodity program policy.

Direct payments. Although once thought to be protected from WTO scrutiny because they were generally decoupled from production, direct payments are no longer shielded from challenge after the Brazil cotton case ruled that the fruit and vegetable limitations do have an effect on production decisions, and thus cannot be categorized in the green box.[76] A supposed easy way to address the problems with direct payments would be to remove the fruit and vegetable restrictions. Such action may affect the political balance between commodity producers and fruit and vegetable growers so that more research or risk management money will be provided to the fruit and vegetable sector.

While direct payments are generally popular with producers and landowners with acreage and yield base, members of the general public can look at these payments with a jaundiced eye. It can be difficult for policy makers to make the typical arguments in support of subsidies for direct payments because: (1) the payments do not necessarily provide a safety net for producers from the inherent risks in farming because the payments are not based on the exigencies of Mother Nature or the market; and (2) the payments provide relatively minimal apparent public benefit by requiring minimal conservation requirements, unlike other conservation based payments such as the Conservation Reserve Program, Conservation Security Program, or Environmental Quality Incentive Program, which require extensive conservation efforts.

Nevertheless, policy makers are sure to look at direct payments as a key component of the next Farm Bill because producers see these payments as providing them the greatest amount of flexibility in planting decisions.

Countercyclical payments. Many believe countercyclical payments are also likely to fall into the amber box.[77] Although one could argue that they do not affect production because the payment does not depend on a farmer producing a crop, they are dependant on market prices and thus likely fall out of the green box.[78] U.S. negotiators, however, have discussed changing the Agreement on Agriculture in the Doha Round to make it clear that CCP's would be included in a category that would not go toward the Aggregate Measure of Support, such as the blue box. CCP's have become popular with producers because they do provide the formulized safety net that was lacking in the 1996 Farm Bill.

Marketing loan programs. The payments that clearly fall within the amber box are the marketing loan gains, loan deficiency payments, and commodity certificates.[79] Producers have come to rely on these payments as providing a price floor for their commodities. If the Doha Round and the new Farm Bill do not somehow move direct payments or countercyclical payments out of the amber box, policy makers may need to consider decreasing the amount of marketing loan payments. Otherwise, the U.S. will risk exceeding the WTO allowable Aggregate Measure of Support and open itself to more WTO challenges.

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Farm Bill/Cont. from page 5

Conservation measures. Many observers argue that the answer to the WTO dilemma is to increase conservation spending and decrease spending on commodity programs. One program in particular, the Conservation Security Program,[80] might provide a vehicle for increased spending on water quality and soil conservation because it pays farmers to engage in these practices on working lands. CSP was new in the 2002 Farm Bill, and although it has suffered some setbacks because of funding and limited availability, the program continues to be popular among producers because all producers, no matter what they grow, are eligible.

Other conservation programs, such as Environmental Quality Incentives Program[81] and the Grassland Reserves Program,[82] also provide farmers incentives to engage in conservation practices. These two programs, along with CSP, tend to garner more support among producers because they allow the producers to continue using the land to gain income. Another widely used program, the Conservation Reserve Program,[83] is more popular with environmentalists and outdoor enthusiasts because it takes land out of production and preserves the land almost exclusively for conservation and wildlife purposes.

Rural development. Beyond conservation, people are also considering whether some of the commodity program resources could be diverted to rural development programs. These programs either assist in bolstering the infrastructure of rural communities or helping rural businesses start up. For example, program in the 2002 Farm Bill called a Value Added Producer Grants provides assistance for business planning as well as capital infusion for promising businesses in rural areas.

A particular area that has garnered a lot of interest is helping businesses that produce biobased products, such as fuel or plastics made from corn or lubricants made for soybeans. As domestic policy makers search for ways for the U.S. to become more energy independent, they are looking to promote domestic biobased energy such as ethanol or soydiesel.

Most of the rural development programs are safe from WTO scrutiny because they fall squarely in the green box. Certain provisions, however, especially those related to bioenergy, could run into WTO restrictions. For instance, some are concerned that the increased demand for ethanol resulting from a recent federal mandate[84] requiring the petroleum industry to increase their use of renewable fuels from 4 billion gallons a year in 2003 to 7.5 billion gallons a year in 2007 may cause an influx of imported ethanol.[85] In response to these new imports, some in Congress have considered policies to ensure that the increased demand will benefit domestic producers. Such policies could include requirements that certain refineries or processors use domestic commodities. Policies that expressly prefer domestic products over exports could run afoul of trade obligations.[86]

Payments related to decreased production. Another approach would hearken back to pre-1996 policy that used land idling in conjunction with government-owned reserves. Essentially, the program would continue to utilize the non-recourse marketing loans and would accept forfeited grain into farmer-owned storage facilities when the loan rate exceeded the market price.[87] The program would pay farmers to store the grain and would release the grain when market prices reached a higher level. To encourage higher prices, Congress would give the Secretary of Agriculture the power to manage supply by requiring farmers who participate in the program to set aside land in times of surplus.[88] The apparent advantage to this program is that it builds reserves for weather disasters and it is designed to let the Secretary use supply management so that the market clears the surplus. Deficiency payments that acted much like the 2002 Farm Bill countercyclical payments provided farmers further protection from low prices. Critics of this approach feared that the reserve served as a drag on the market because global buyers always figured in the excess supply into pricing decisions. Furthermore, some criticized the level of involvement the government had in production decisions.

Certain parts of this approach, such as the target payments, would likely fall into the blue box because the target payments could be conditioned on the producers agreeing to limit their production per USDA's determination. It is less clear how the WTO would treat the government storage program because the system is designed to affect prices by tamping down price spikes and leveling off price valleys.

Buyouts and state block grants. Two less likely, but interesting, scenarios are the use of buyouts or state block grants. One could look to the tobacco buyout in the 2002 Farm Bill for an example of how Congress could decide to eventually discontinue domestic support, but compensate landowners and producers who have invested in the sector assuming that the subsidies would continue.[89] Such an approach would likely look to acreage and yield bases, much like the direct payment formula, to determine a lump sum payment to producers. Obviously this approach has appeal to those who would like to see the subsidies terminated. It is unlikely that such a buyout would violate WTO obligations because the buyout would not directly affect production decisions.

Another novel idea would take the budget for commodity programs and dispense it to the states in the form of block grants. The states could then decide how to support farmers and rural communities. This approach raises a myriad of question, most significantly: How would the money be divided? What restrictions would be put on states? Where would the states spend the money? How a WTO panel would view this idea would likely depend on whether the states decide to implement programs that would affect production or distort world market prices.

Conclusion

Trade policy has always played a major role in the evolution of the U.S. agricultural sector. With the 1994 Agreement on Agriculture resulting form the WTO Uruguay Round, trade policy started to play an even more important role in domestic farm policy. As we move deeper into 2006, the intersection of these two policies becomes more prominent with the negotiations of the Doha Round that may result in a new WTO agreement on agriculture. If the Doha Round fails, Congress will need to consider the implications of the Brazil Cotton Case and whether current policy may open the U.S. to more WTO challenges. No one can predict the result of this geopolitical chess match, but one can assume that the agricultural policy landscape is poised to change in the next few years.

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[1] For an excellent extended explanation of these mechanisms, see Jim Monke, *Farm Commodity Programs: Direct Payments, Counter-Cyclical Payments, and Marketing Loans*, Congressional Research Service (Feb. 10, 2006), at http://www.nationalaglawcenter.org/assets/crs/RL33271.pdf.

[2] In general, the commodities covered by the commodity programs include wheat, corn, grain sorghum, barley, oats, upland cotton, rice, soybeans and other oilseeds. 7 U.S.C. § 7901(4). These commodities are eligible for all three types of payment mechanisms. Certain other commodities, known as loan commodities, are not eligible for direct payments and counter cyclical payments, but are eligible for loans, they include extra long staple cotton, wool, mohair, honey, dry peas, lentils, and small chickpeas. 7 U.S.C. § 7901(8).

[3] 7 U.S.C. § 7901(12).

[4] 7 CFR part 1400 subpart C is devoted exclusively to the phrase.

[5] 7 CFR 1400.201(b).

[6] 7 U.S.C. § 7915(a)(A); 16 U.S.C. § 3811.

[7] 7 U.S.C. § 7915(a)(B); 16 U.S.C. § 3821.

[8] 7 U.S.C. § 7911(a).

[9] 7 U.S.C. § 7912.

[10] 7 CFR 1400.1(g).

[11] For an excellent explanation of the rules affecting payment limitations, see Christopher R. Kelley, *Introduction to Federal Farm Program Payment Limitation and Payment Eligibility Law*, National Agricultural Law Center (2002), at http://www.nationalaglawcenter.org/assets/articles/kelley_paymentlimitations.pdf.

[12] The term "covered commodity" includes wheat, corn, grain sorghum, barley, oats, upland cotton, rice, soybeans, and other oilseeds. 7 U.S.C. § 7901(4). All of these commodities are eligible for direct payments, countercyclical payments and marketing loans. Certain other commodities, "loan commodities", are eligible for

Farm Bill/Cont. from page 6
marketing loans only, including: wool, mohair, honey, dry peas, lentils, and small chickpeas. 7 U.S.C. § 7901(8).

[13] 7 U.S.C. § 7916.

[14] *See* notes 8 thru 9 and accompanying text.

[15] 7 U.S.C. § 7913(b) (providing payment rates for covered commodities).

[16] 7 U.S.C. § 7914(c).

[17] 7 U.S.C. § 7932 provides loan rates for covered commodities and loan commodities.

[18] 7 U.S.C. § 7934.

[19] 7 U.S.C. § 7935.

[20] WTO website, The WTO in Brief, at http://www.wto.org/english/thewto_e/whatis_e/inbrief_e/inbr00_e.htm.

[21] WTO website, WTO Fact File, at http://www.wto.org/english/thewto_e/whatis_e/whatis_e.htm.

[22] WTO website, Understanding the WTO: The Agreements, at **http://www.wto.org/english/thewto_e/whatis_e/tif_e/agrm1_e.htm.**

[23] Organization for Economic Cooperation and Development (OECD), *The Uruguay Round Agreement on Agriculture: An Evaluation of its Implementation in OECD Countries* 5 (2001), at http://www.oecd.org/dataoecd/50/55/1912374.pdf.

[24] WTO Agreement on Agriculture (1994) (Agreement on Agriculture), different electronic versions of Agreement on Agriculture can be found at http://www.wto.org/english/docs_e/legal_e/legal_e.htm#ag.

[25] *Id.*, Article 4.2.

[26] Although the phrase 'domestic support' is not defined in the Agreement on Agriculture, a definition can be inferred from the definition of Aggregate Measure of Support, which includes "support, expressed in monetary terms, provided for an agricultural product in favour of the producers of the basic agricultural product or non-product-specific support provided in favour of agricultural producers in general …" *Id.*, Article 1(a).

[27] Randy Schnepf, *Agriculture in the WTO: Policy Commitments Made Under the Agreement on Agriculture*, Congressional Research Service 6 (May 12, 2005) (hereinafter WTO Commitments), at http://www.nationalaglawcenter.org/assets/crs/RS20840.pdf.

[28] Randy Schnepf, *Agriculture in the WTO: Limits on Domestic Support*, Congressional Research Service 6 (May 10, 2006) (hereinafter WTO Limits), at http://www.nationalaglawcenter.org/assets/crs/RS20840.pdf.

[29] Agreement on Agriculture, *supra* note 25, Article 6.5.

[30] *Id.* Annex 2, § 2.

[31] *See supra* notes 56 to 62 and accompanying text.

[32] Agreement on Agriculture, *supra* note 25. Article 6.4.

[33] WTO Limits, *supra* note 28, at 2.

[34] WTO Commitments, *supra* note 27, at 9; *see* Chuck Culver, *Glossary of Agricultural Production, Programs, and Policy* (4th Ed.), at http://www.nationalaglawcenter.org/# (defining export subsidy as "[s]pecial incentives (such as cash payments, tax exemptions, preferential exchange rates, and special contracts) extended by governments to encourage increased foreign sales. These subsidies are most often used when internal prices exceed export prices."); Agreement on Agriculture, *supra* note 24, Article 1(e) (defining export subsidies as "subsidies contingent upon export performance.").

[35] WTO Commitments, *supra* note 27, at 10. Certain exemptions apply, such as bona fide food aid. Agreement on Agriculture, *supra* note 25, at Article 10.4.

[36] Developing countries agreed to a 24% reduction over ten years. WTO Commitments, *supra* note 28, at 10.

[37] Article 1.1. the SCM Agreement defines "subsidies" as a financial contribution by a government where a benefit is conferred. WTO Agreement on Subsidies and Countervailing Measures (1994) (hereinafter Agreement on SCM).

[38] Agreement on Agriculture, *supra* note 24, Article 13.

[39] The WTO website summarizes treatment of actionable subsidies:

"[T]he complaining country has to show that the subsidy has an adverse effect on its interests. Otherwise the subsidy is permitted. The agreement defines three types of damage they can cause. One country's subsidies can hurt a domestic industry in an importing country. They can hurt rival exporters from another country when the two compete in third markets. And domestic subsidies in one country can hurt exporters trying to compete in the subsidizing country's domestic market. If the Dispute Settlement Body rules that the subsidy does have an adverse effect, the subsidy must be withdrawn or its adverse effect must be removed. Again, if domestic producers are hurt by imports of subsidized products, countervailing duty can be imposed."

WTO Website, Anti-dumping, Subsidies, Safegaurds: Contingencies, etc., at http://www.wto.org/english/theWTO_e/whatis_e/tif_e/agrm8_e.htm.

[40] *Id.* Article 3.

[41] *Id.*

[42] Karen Halverson Cross, *King Cotton, Developing Countries, and the 'Peace Clause': The WTO's Cotton Subsidies Decision*, 9 J. of Int'l Econ. L. 149, 163 (2006).

[43] Agreement on SCM, *supra* note 37, Article 6.3.

[44] Cross, *supra* note 42, at 163.

[45] Agreement on Agriculture, *supra* note 24, Article 13.

[46] *See id.*, Article 13 (extending the Peace Clause through the implementation period); and Article 1(f) (defining "implementation period" for purposes of Article 13 as "the nine year period commencing in 1995").

[47] *Id.*, Article 13(b).

[48] *Id.*, Article 13(a).

[49] *Id.*, Article 13(c).

[50] WTO, *Dispute Settlement Understanding* (hereinafter DSU) (1994) (Annex 2 of 1994 GATT). A number of electronic versions of the DSU can be found at http://www.wto.org/english/docs_e/legal_e/legal_e.htm#dispute.

[51] *Id.*, Article 4.

[52] *Id.*, Article 6.

[53] *Id.*, Article 17.

[54] *Id.*, Article 22.

[55] For a summary of the WTO Cotton dispute (DS267) and a link to numerous documents related to the case, see WTO Website, United States Subsidies on Upland Cotton, at http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds267_e.htm.

[56] Chuck Culver, *Glossary of Agricultural Production, Programs, and Policy* (4th Ed.), at http://www.nationalaglawcenter.org/#. The Step 2 program is codified at 7 U.S.C. § 1207.

[57] WTO Agreement on Subsidies and Countervailing Measures, Article 3.1. For links to different electronic versions of the Agreement, go to http://www.wto.org/english/docs_e/legal_e/legal_e.htm#subsidies.

[58] Randy Schnepf, *Background of the U.S.-Brazil WTO Cotton Subsidy Dispute*, Congressional Research Service 15 (July 11, 2005), at http://www.nationalaglawcenter.org/assets/crs/RL32571.pdf.

[59] P.L. 109-171, sec. 1103. The repeal was included in the Budget Reconciliation bill signed on February 8, 2006.

[60] Agreement on Agriculture, *supra* note 24, Article 13.

[61] Randy Schnepf, *Background of the U.S.-Brazil WTO Cotton Subsidy Dispute*, Congressional Research Service 15 (July 11, 2005), at http://www.nationalaglawcenter.org/assets/crs/RL32571.pdf.

[62] *Id.* at 15.

[63] Agreement on Agriculture, *supra* note 24, Article 20.

[64] WTO, Doha Ministerial Declaration (Nov. 14, 2001) (hereinafter Doha Ministerial). Links to this declaration and supporting documents can be found at http://www.wto.org/English/tratop_e/dda_e/dda_e.htm.

[65] Doha Ministerial, *supra* note 64, para. 2. The focus on developing countries includes an express intention to provide these countries special and differential treatment in the trade agreement. *Id.* at para 13.

[66] Charles Hanrahan and Randy Schnepf, *WTO Round: The Agricultural Negotiations*, Congressional Research Service 16 (Jan. 12, 2006), at http://www.nationalaglawcenter.org/assets/crs/RL33144.pdf.

[67] Doha Ministerial, *supra* note 64, para. 45.

[68] WTO, Hong Kong Ministerial Declaration, (Dec. 18, 2005), paras. 1 and 10, at http://www.wto.org/english/thewto_e/minist_e/min05_e/final_text_e.html.

[69] Charles Hanrahan and Randy Schnepf, *WTO Round: The Agricultural Negotiations*, Congressional Research Service 19 (Jan. 12, 2006), at http://www.nationalaglawcenter.org/assets/crs/RL33144.pdf; *see* European Union News Release, *WTO Farm Talks: EU Commissioner Fischler Vows to Plow On* (Mar. 31, 2003), which provides:

Modalities will indicate the general objectives (including numerical targets as well as rules) and the way to achieve them. For example, as regards tariff reductions, a modality would be an average reduction of 36% with a minimum 15% reduction per tariff line to be reached by, for example, 6% reduction over six years.

Modalities also comprise all the detailed rules to be incorporated in the WTO Agreement on Agriculture, be it new rules (as for example the EC is pursuing on export credits, food aid and geographical indications) or amendments to existing rules (as for example on domestic support where the EU wants to include animal welfare under the "green box"), or an effort to reach an agreed understanding, as for example on food safety and the use of the precautionary approach.

[70] 19 U.S.C. § 3803.

[71] *Id.*

[72] Some point out that it is in Congress purview to extend TPA. This paper acknowledges that possibility but does not make that assumption.

[73] Forrest Laws, *Johanns Says No to Farm Bill Extension*, Western Farm Press (Mar. 6, 2006).

[74] *The Kiplinger Agricultural Letter* (Mar. 3, 2006). This newsletter predicts that the 2002 Farm Bill will be extended, though not until mid-2007. The article points out that many farm groups would prefer to have the next Farm Bill debated in 2008, a presidential year when federal candidates tend to be more sensitive to certain constituencies.

[75] Oxfam International, *Truth or Consequence: Why the EU and the USA Must Reform Their Subsidies, or Pay the Price* 15-17 (Nov. 2005), at http://www.oxfam.org.uk/what_we_do/issues/trade/bp81_truth.htm.

[76] *See supra* notes 55 to 62 for a discussion on the how the Brazil Cotton Case considered direct payments.

[77] *See supra* note 16 and accompanying text (explaining countercyclical payments).

[78] Agreement on Agriculture, *supra* note 24, Annex 2, 1(b) provides that a domestic support measure may not be exempt from reduction commitments if it has "the effect of providing price support to producers."

[79] The U.S. has reported marketing loan benefits in the amber box. Randy Schnepf, *Agriculture and the WTO: Limits on Domestic Support*, Congressional Research Service 6 (May 10, 2005), at http://www.nationalaglawcenter.org/assets/crs/RS20840.pdf.

[80] 16 U.S.C. § 3838.

[81] 16 U.S.C. § 3839aa.

[82] 16 U.S.C. § 3838n.

[83] 16 U.S.C. § 3831.

[84] P.L. 109-058 (Aug. 8, 2005).

[85] *See* Joel Severinghaus, *Why We Import Brazilian Ethanol*, Iowa Farm Bureau Federation, at http://www.iowafarmbureau.com/programs/commodity/information/pdf/Trade%20Matters%20column%20050714%20Brazilian%20ethanol.pdf (answering the title's question: "Simple economics: U.S. ethanol demand now exceeds U.S. ethanol supply, so imports will make up the difference. And Brazil can produce ethanol from sugarcane more cheaply than we can make it from Iowa corn.").

[86] General Agreement on Tariffs and Trade (1947), Article III generally provides that nations must not favor domestic products over foreign products.

[87] Tracy Bruckner, *et al.*, *Toward a Global Food and Agriculture Policy*, Leopold Center for Sustainable Agriculture (Jan. 2005), at http://www.leopold.iastate.edu/pubs/staff/policy/globalag.pdf.

[88] *Id.*

[89] *See generally* Jasper Womach, *Comparing Quota Buyout Payments for Peanuts and Tobacco*, Congressional Research Service (Oct. 14, 2003), at http://www.nationalaglawcenter.org/assets/crs/RS21642.pdf.

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AMERICAN AGRICULTURAL LAW ASSOCIATION NEWS

AALA member Paul Wright to be inducted into the Ohio Agricultural Hall of Fame. By Peggy Kirk Hall
The Ohio Agricultural Council recently announced Paul's selection for the Agricultural Hall of Fame, Ohio's highest recognition for individuals who have made outstanding contributions to the agricultural industry. Paul will be inducted at a special ceremony at the 2006 Ohio State Fair that will highlight his accomplishments, service and leadership throughout his career. Paul played a founding role with the American Agricultural Law Association and was the first Ohio attorney chosen to serve as President of AALA. "Paul has been a valuable, respected member of AALA as long as I have known him," stated AALA President Don Uchtmann. Many other "firsts" are included in Paul's long list of accomplishments: serving as the first Farm Management Specialist and Associate Professor to specialize in agricultural law at The Ohio State University—where he established OSU's Agricultural Law Center and taught OSU's first course in Agricultural Law—and founding Wright Law Company, one of the first Ohio law firms to cater to the needs of agriculture. Paul will also be recognized for a lengthy record of service and mentoring to the legal profession, OSU and his church community. "Paul has had a tremendous positive influence on agricultural law and the agricultural interests in Ohio and beyond," according to Ohio attorney Larry Gearhardt—"He is the 'Godfather' of agricultural law in Ohio."

Nominations for Annual Scholarship Awards. The Scholarship Awards Committee is seeking nominations of articles by professionals and students for consideration for the annual scholarship awards presented at the annual conference. Please contact Jesse Richardson, Associate Professor, Urban Affairs and Planning, Virginia Tech, Blacksburg, Virginia 24061-0113,(540) 231-7508 (phone) (540) 231-3367 (fax) email: jessej@vt.edu

New AALA Website design. Many thanks to Greg Deane of Diving Turtle Designs in Eugene, OR for redesigning, visually as well as technically, the AALA web site. Greg donated, and continues to donate, a substantial amount of time to the project in addition to the contracted services. The next phase of development will be to add functionality to the site to give members more control over their information in the database, the ability to search the *Update* archives, and the ability to pay dues and registration fees by credit card using Paypal. Please take a moment to view the site and to send me any comments. The site is designed to work with all browsers but one never knows where a problem may arise.

--Robert P. Achenbach, Jr, AALA Executive Director P.O. Box 2025, Eugene, OR 97405 541-485-2090 RobertA@aglaw-assn.org