

Special Article

Agriculture & the Evolution of Tariff Bargaining

Preparations have already begun for the ninth round of international trade talks, which will be launched at the World Trade Organization (WTO) Ministerial Conference in Seattle this December. While agriculture had been included in each of the previous rounds, it was not until the Uruguay Round of Multilateral Trade Negotiations (1986-94) that real progress was made in negotiating overall reductions in barriers to agricultural trade. The Uruguay Round created the WTO, which replaces the General Agreement on Tariffs and Trade (GATT) as an institutional framework for overseeing trade negotiations and adjudicating trade disputes.

Over the course of the previous eight rounds, countries successfully lowered tariffs for manufactured goods from a trade-weighted, most-favored-nation (MFN) average of over 40 percent to about 4 percent. A review of how this was accomplished reveals some valuable lessons for future negotiations aimed at achieving similar cuts in agricultural tariffs, which are, on average, still much higher than those on manufactured items.

Tariff Bargaining in Previous Rounds

A variety of bargaining approaches has been used in previous trade rounds. In the first round (*Geneva*, 1947), negotiations took a bilateral approach, despite the multilateral setting.

Each country drafted request-and-offer lists that contained the tariffs it would like other countries to reduce and/or bind and the concessions it was willing to make in exchange. (Tariffs are “bound” when a country agrees not to raise them above a certain level, subject to a penalty). Negotiations were conducted country-by-country and item-by-item, focusing on products for which the two countries were mutual principal import suppliers. Early on, countries agreed that they would extend concessions to all participants, whether or not those countries made any reciprocal concessions, thus ensuring that the negotiations achieved some of the benefits of multilateralism. This practice, now codified in the GATT’s most-favored-nation clause, ensured that concessions between principal suppliers would not discriminate against other suppliers.

The first round reduced average U.S. industrial tariffs by almost 20 percent. About 54 percent of U.S. dutiable imports were subjected to tariff cuts, with the weighted-average reduction equal to 35 percent. Even though the MFN practice meant that the benefits of concessions could not be restricted to principal suppliers, they were kept largely among the negotiating parties. For example, an estimated 84 percent of U.S. imports subjected to tariff cuts came from the 22 other participants in the negotiations.

This is the first of two articles on tariffs and the World Trade Organization (WTO). The second will profile tariff schedules of selected WTO members.



Ianina Iang, World Trade Organization

Measured in terms of trade volume subjected to tariff concessions and the average depth of tariff reduction achieved, the next four rounds of negotiations yielded disappointing results. For the U.S., these rounds achieved average tariff reductions between just 2 and 4 percent on dutiable imports. Among the reasons for the poor outcomes were the limited objectives of some of the rounds and the limited authority accorded to U.S. negotiators by Congress.

The request-and-offer form of negotiating also largely inhibited the success of these rounds. As more countries joined the talks, negotiating item-by-item with principal suppliers proved to be increasingly slow and cumbersome, making further cuts in tariffs more difficult to achieve. It also became increasingly difficult for negotiators to monitor the multilateral balancing possibilities on thousands of items for dozens of countries.

Many of the tariffs that had been cut in the early rounds continued to be high enough to provide a comfortable cushion against import competition. As this cushion was slowly removed, the protected industries, which had come to rely on the higher prices generated by tariffs, began vigorously to resist further tariff reductions.

By continuing the strategy of negotiating reciprocal concessions with other main trading partners, governments sought to assure their constituents that the economy as a whole would not lose by binding or lowering tariffs. The principal-supplier method of negotiating supported the pervasive belief that every dollar increase in imports should be balanced with a dollar

increase in exports. Reducing one's trade barriers was considered a concession that had to be compensated by equivalent concessions from other countries, a tenet that continues to influence today's negotiations.

While tariffs on industrial goods were whittled away during the first five rounds, the issue of agricultural trade barriers was scarcely touched. Agricultural trade was subject mainly to non-tariff barriers (NTB's) such as quotas, many of which were tied to specific domestic policy objectives. Their removal or reduction would have required changes in domestic policies as well, something few countries were willing to address in what essentially were trade talks.

The sixth round, dubbed the *Kennedy Round* (1963-67), saw the first serious attempt to subject agricultural products to disciplines that had been applied to trade in other goods for many years. Before the round began, the U.S. suggested that all NTB's in agriculture be converted to tariffs, which would then be reduced by 50 percent and bound. This position—which never made it into the U.S. proposal—was considered a non-starter by the European Economic Community because it was incompatible with the use of variable levies (under which the import duty is the difference between a fixed reference price and a fluctuating import price). In the end, even though agriculture had been given high priority during the Kennedy Round, little was accomplished in liberalizing agricultural trade.

In contrast to the efforts for agriculture, negotiations to reduce tariffs on industrial goods were highly successful, in large part because of a major shift from a bilateral to a multilateral negotiating approach. Early in the round, participants agreed to a 50-percent across-the-board reduction in industrial tariffs for all but a bare minimum of protected products. They then negotiated further exceptions.

This approach gave an early boost to the negotiations by providing an initial major step forward, then focused the round on negotiating minor steps backward. Compared with the modest cuts achieved by the principal-supplier, item-by-item approaches of the previous rounds, this approach, even after all the exceptions were negotiated, succeeded in reducing industrial country tariffs on manufactured items by an impressive 35 percent on average.

In the seventh round, the *Tokyo Round* (1973-79), the across-the-board reduction technique (with exceptions) was continued, although considerable debate surrounded the choice of tariff-cutting formula to be used. One of the problems, whose roots could be traced in part to the principal-supplier approach to negotiating tariff reductions, was that many countries now had significant dispersion across their industrial tariff rates, meaning a low overall average coupled with occasional very high rates, or tariff peaks. In the past, when a country had tariffs that were sufficiently high to preclude any trade taking place, there was no principal-supplier with which to negotiate reductions. And since countries tended to be strongly influenced in their negotiations by

the amount of actual trade subject to the tariff barrier being discussed, these high tariffs might escape any cuts. Actual, rather than potential, trade was much more influential in determining which tariffs would be targeted for reduction, since it provided a convenient way to estimate costs and benefits of the negotiations.

To address the tariff dispersion that existed, the European Community proposed that, instead of a linear cut as imposed by the Kennedy Round, a nonlinear "harmonization formula" be used. This formula yielded small average cuts, but included deeper cuts for higher tariff rates. The U.S., however, preferred a larger, but equal cut in tariffs. The Tokyo Round languished for over 2 years, until a compromise tariff-cutting formula (the Swiss formula) reduced tariff disparities between and within countries. As a result of this compromise, the Tokyo Round succeeded in cutting global industrial tariffs an estimated 30-35 percent, and the MFN tariff rates on imports of manufactured items were estimated to average 4.9 percent in the U.S., 6 percent in the European Community, and 5.4 percent in Japan.

The Tokyo Round was notable in several other respects. It was the first round to formally recognize that trade flows are affected by the close link between domestic and trade policies. Acknowledging this connection laid the groundwork for steps that would be taken in the Uruguay Round to begin reducing protection in the agricultural sector. It also introduced the sectoral approach to negotiating, in which barriers to trade affecting a particular sector would be discussed in isolation rather than in conjunction with all sectors. This approach, while not successful in reducing agricultural trade barriers during the Tokyo Round, would be used again in the *Uruguay Round* (1986-94) to finally subject agricultural trade to the sorts of disciplines that had applied to other traded goods for many years.

The success of the Uruguay Round is predicated largely on its treatment of NTB's in the agricultural sector. Since the early years of the GATT, NTB's had been regarded as much more trade restricting in agriculture than tariffs. More than 30 years had passed since the U.S. had first proposed in the GATT that agricultural NTB's be converted to tariffs before the signatories to the Uruguay Round Agreement on Agriculture (URAA) agreed to do just that. Countries further agreed that these new tariffs, as well as any other existing tariffs, would be progressively reduced to a final, bound rate.

The guidelines used, both for calculating the tariff equivalent of existing NTB's and for reducing tariffs, offered broad accommodations for countries to design tariff structures that would provide ample protection for politically sensitive commodities while concentrating cuts on commodities which they themselves were not producing or were not producing on a competitive basis. (For an explanation of how "tariffication" was achieved, see AO December, 1998). Nevertheless, simply replacing NTB's with nondiscriminatory bound tariffs was a huge step forward. It served to renew and affirm each member country's commitment to GATT principles and set the stage for negotiation of further cuts in agricultural tariffs.

Special Article

Highlights of Tariff Negotiations Through the Uruguay Round

<i>Round, date</i>	<i>Main accomplishments</i>	<i>Agricultural milestones</i>
Geneva (1947), Annecy (1949), Torquay (1950-51), Geneva (1955-56)	During the first four rounds, negotiations are based on request-and-offer lists, with countries first negotiating bilaterally with principal suppliers then exploring possible multilateral balancing opportunities.	In the fourth round, the U.S. obtains a waiver to impose quantitative restrictions for commodities covered under Section 22 of the Agricultural Adjustment Act.
Dillon Round (1960-62)	The first round after the formation of the European Community (EC), this was the last round to use the request-and-offer approach to negotiating.	The EC makes concessions to allow duty-free bindings (setting tariffs that cannot be increased without notification and compensation) on soybeans, soymeal and corn gluten feed and low-duty bindings on soybean oil, other oilseeds and products, and cotton.
Kennedy Round (1963-67)	For first time, tariff negotiations are conducted across-the-board, rather than item-by-item. Participants agree early on to an overall linear tariff-cutting formula of 50% and then negotiate exceptions. The contentious issue of tariff disparities is left for the next round.	Ag negotiations center on basic mechanisms of the EC's Common Agricultural Policy. EC suggests binding margins of producer price support in relation to world reference prices. This approach is rejected and ag negotiations end stalemated. The International Wheat Council and the Food Aid Convention are created.
Tokyo Round (1973-79)	Debate is considerable on tariff-cutting formula to be used to reduce disparity across tariffs. EC proposes a nonlinear formula designed to combine small average cuts with larger cuts for higher tariff rates. U.S. prefers larger but equal percentage cuts. A compromise, the Swiss formula, is applied to reduce tariff disparities between and within countries, with negotiated exceptions.	In a significant departure from previous rounds, agriculture is identified as a separate agenda item. Several countries favor subjecting it to the same disciplines as the industrial sector. In the end, this is not done. The only improvement in market access is a limited number of small tariff concessions and import quota enlargements resulting from traditional request-and-offer negotiations.
Uruguay Round (1986-94)	This is the most comprehensive round to date. Major players agree that the results for nonagricultural tariffs aim to be at least as ambitious as the Tokyo Round (i.e., one-third reduction). The most ambitious agreement is to completely eliminate tariffs in certain sectors (including pharmaceuticals; steel; furniture; beer; spirits; and agricultural, construction, and medical equipment) and to harmonize tariffs on chemicals.	Nontariff barriers are converted to tariffs equal to the difference between internal and external prices existing during 1986-88. All tariffs are bound and cut by a minimum of 15%, with the average reduction over all agricultural tariffs to equal 36%, on a simple average (unweighted) basis for developed countries.

Maintaining Momentum for the Next Round

Although the scope of the next round of talks is yet to be defined, agriculture will once again have a central place on the agenda. As part of the URAA, countries agreed to begin negotiations by the end of 1999 in order to continue the process of substantially reducing support and protection in the agricultural sector. Agricultural negotiations are expected to focus on continuing the reform process which began under the Uruguay Round by expanding market access, reducing or eliminating export subsidies, and further disciplining the use of trade-distorting domestic subsidies.

In the area of market access, the weight of remaining protection has now shifted toward tariffs, some of which are extremely high (although there is growing concern about technical barriers to trade). Negotiators will confront the task of addressing these high tariffs. Of course, not all countries have high agricultural tariffs, nor are all agricultural commodities subject to high tariffs. So, while the overall level of protection is high relative to that in manufacturing sectors, it is also highly uneven across countries and commodities.

Based on the level of cuts in tariffs on manufactured goods achieved in past rounds, an across-the-board approach has achieved the greatest success. If all parties were to make an early commitment to a significant across-the-board cut in tariffs—no country has done so—negotiators would likely concentrate on other issues of contention in the agricultural sector. Some observers have suggested simply repeating the level of tariff cuts of the last round, which equaled 36 percent on average. Early acceptance of such a proposal might allow cuts to be implemented soon enough to provide a seamless continuation of the URAA reforms. (The last installments of tariff reductions are in 2000 for developed countries.)

Tariff escalation—when tariffs are low or zero on primary products, then increase as the product undergoes additional processing—can be a significant bias against trade of the processed product. If countries cut the rates on raw materials by a greater amount than the processed product, this could increase the level of tariff escalation. Should countries agree to an initial across-the-board cut in tariffs but then negotiate exceptions, minimizing exceptions in those cases where tariffs are already very high is another option.

Some observers have advocated that tariff dispersion and escalation be reduced through a harmonization formula, as used in the Tokyo Round, to subject higher tariffs to larger percentage cuts. However, past experience shows that reaching agreement on a formula would also require a great deal of negotiation.

One drawback to a linear tariff cut is that it does not reduce the dispersion of tariffs. On the other hand, it does reduce dispersion of import prices. For example, a 50-percent cut in tariffs yields a 2.4-percent cut in the import price when the initial tariff equals 5 percent, and yields a 16.7-percent cut in the import price when the tariff equals 50 percent. Therefore, the potential increase in imports is likely to be proportionately larger for countries with high tariffs than for those with low tariffs when both groups reduce tariffs by the same percentage. The exception is when even a large cut in a tariff still results in a rate high enough to prohibit imports from taking place.

The history of past GATT rounds reveals how negotiating approaches have changed through the years. The earliest rounds adopted a bilateral negotiating stance conducted on an item-by-item basis. As the number of countries participating in negotiations increased, the focus switched from resolving issues that mainly affected mutual trade between principal suppliers, to achievement of a multilateral balance of concessions. At the same time, the negotiating approach changed from item-by-item to an across-the-board basis. Later talks experimented with sector-by-sector approaches to bargaining.

Unlike the early rounds, which benefited from an overriding objective to reduce and bind tariffs, later rounds have been increasingly broad and complex, encompassing more participants and issues. What all rounds have had in common, however, is a tendency for the pursuit of reciprocity to govern the size and extent of tariff cuts countries are willing to concede.

The URAA would have been less successful if it had not been part of an overall package of results addressing a wide range of issues and sectors. The challenge this time will be to set up a broad-based but manageable process that yields results in a short time period (e.g., 3 years) in order to avoid losing the momentum of reforms generated by the Uruguay Round. **AO**

John Wainio (613) 759 7452
jwainio@econ.ag.gov



Visit the WTO Briefing Room

on the [Economic Research Service website](http://www.econ.ag.gov)

Learn more about tariffication, tariff reduction, and other WTO topics

www.econ.ag.gov/briefing/wto/