United States General Accounting Office 152485

GAO

Briefing Report to the Honorable Thomas A. Daschle, U.S. Senate

August 1994

INTERNATIONAL TRADE

Impact of the Uruguay Round Agreement on the Export Enhancement Program

Notice: This is a reprint of a GAO report.

GAO

United States
General Accounting Office
Washington, D.C. 20548

General Government Division

B-257783

August 5, 1994

The Honorable Thomas A. Daschle
United States Senate

Dear Senator Daschle:

Seven years of negotiations culminated recently in the Uruguay Round of the General Agreement on Tariffs and Trade (GATT), whose signatories agreed, among other things, to discipline the use of trade-distorting practices, such as tariffs and subsidies. You asked us to provide information on the likely impact of the Uruguay Round agreement on U.S. agricultural export programs—primarily, the U.S. Department of Agriculture's (USDA) Export Enhancement Program (EEP). Specifically, our objectives were to identify (1) the likely impact the Uruguay Round agreement would have on U.S. agricultural export programs and (2) the proposals by industry participants and interest groups that the Congress could consider for making legislative changes to EEP and other agricultural trade programs managed by USDA's Foreign Agricultural Service (FAS).

We provided a briefing to you on July 19, 1994. This report summarizes the substance of that briefing.

Results in Brief

The Uruguay Round agreement, if implemented, would require the United States to reduce its agricultural export subsidies, starting in 1995. The required reductions in subsidized exports—36 percent in budgetary outlays and 21 percent in commodity quantities—would be phased in during a 6-year period and would affect several U.S. agricultural export programs, the largest of which is EEP. The reductions would be based on the average budgetary outlays and quantities subsidized during the 1986-90 base years on a commodity-specific basis. Because subsidies for specific commodities have fluctuated since 1990, some commodities would be harder hit—in relation to current levels—than others.

While the Uruguay Round Agreement would not directly restrict USDA's export credit, food aid, or market promotion and development programs, it established guidelines for food aid and market promotion to ensure these programs would not be used to circumvent export subsidy reductions.

In discussions with agricultural interest groups, we identified two specific proposed alternatives to the current EEP program. The World Perspectives, Inc. (WPI),[1] and the National Association of Wheat Growers' (NAWG) proposals differ on the extent of suggested changes to the current EEP program. Both proposals recommend that EEP be expanded to more markets and not just targeted to countries to which the European Union (EU)[2] has subsidized exports. In addition to the two proposals, the Congress is considering legislation proposed by the dairy industry that would establish a marketing board, a concept that other commodity groups are also considering.

In addition, the EEP exporters we contacted made several suggestions on how to improve the current EEP program. Some suggestions dealt with expanding or eliminating the targeting aspect of EEP, while others were intended to make the program more flexible for exporters and buyers. Some of the suggestions called for fundamental change in U.S. agricultural trade policies and the programs designed to implement those policies. However, there was no clear consensus among the exporters we contacted about the continued need for the program or its ideal structure if the Uruguay Round agreement were to be implemented.

FAS is currently preparing a position paper on the implications of the Uruguay Round agreement for EEP. FAS expects to complete the position paper within 2 to 3 months. The position paper will then be used by the National Economic Council to review EEP in light of the Uruguay Round agreement.

The Uruguay Round agreement, if implemented, raises questions as to whether the goals and objectives of EEP need to be revised. Currently, EEP is designed to maintain pressure on our competitors, primarily the European Union, to negotiate agricultural reform. While the Uruguay Round agreement did not eliminate the use of subsidies, the agreement limited the extent to which subsidies can be used. Any consideration of the merits of alternative proposals or significant changes to EEP need to be evaluated against the role and purpose of the program.

Background

The United States has been the largest exporter of agricultural commodities over the past 3 decades. During the early and mid-1980s, however, the United States began to lose some of its share of the world market, partly due to other countries' subsidies of their agricultural exports. The United States then implemented a number of programs, the largest of which is EEP, designed to counter the export subsidy practices of other countries and to maintain and expand U.S. agricultural exports. The major objectives of EEP are to (1) challenge unfair foreign trade practices, such as the use of subsidies; (2) expand U.S. agricultural exports; and (3) encourage other countries exporting agricultural commodities to undertake serious negotiations on agricultural trade problems.

[1]World Perspectives, Inc., is a Washington, D.C.-based agricultural and trade policy consulting firm.

[2]The European Union was formerly known as the European Community. It consists of 12 member countries: Belgium, France, Germany, Italy, Luxembourg, the Netherlands, Denmark, Ireland, the United Kingdom, Greece, Spain, and Portugal.

The Uruguay Round of GATT began in 1986 and concluded on December 15, 1993. The ensuing agreement, signed in Marrakesh, Morocco, on April 15, 1994, sought to liberalize world trade by (1) reducing trade barriers such as tariffs and subsidies; (2) improving GATT as a legal framework; (3) enhancing GATT as an institution, by strengthening the dispute settlement function; and (4) introducing measures to open markets in sectors where GATT disciplines were weak or nonexistent, such as agriculture.

Before the Uruguay Round Agreement can take effect for the United States, the Congress must pass implementing legislation. The Uruguay Round agreement is scheduled to go into effect in July 1995. However, the Director General of GATT is trying to move the effective date up to January 1995.

The Uruguay Round Agreement on agriculture is the beginning of a multilateral process to substantially reduce export subsidies and other activities that distort agricultural trade. To meet this long-term goal, the agreement provides that member nations shall meet in 1999 to review the impact of the Uruguay Round and to negotiate further reductions in export subsidies and other trade-distorting practices.

Scope and Methodology

To identify the likely impact the Uruguay Round agreement would have on U.S. agricultural export programs, we reviewed the final text of the agreement, known as the "Final Act," along with associated documents and country schedules. We also reviewed summaries, studies, and analyses of the agreement prepared by USDA, export organizations, and U.S. foreign trade analysts. The identification of USDA programs affected and unaffected by the export subsidy requirements of the Uruguay Round agreement was based upon USDA's analysis. It does not reflect our independent legal analysis of the Uruguay Round agreement. We did not verify the accuracy of data obtained from FAS showing the impact of the agreement on a commodity-specific basis. We held discussions with USDA staff who had been involved with the negotiations, as well as with other trade experts not affiliated with USDA.

To identify options that could be considered for making legislative changes to EEP, we reviewed EEP's legislative and regulatory histories to determine the goals and objectives of the program. In addition, we held discussions with 17 agricultural interest groups, including industry associations, commodity groups, consultants, and others to identify options for legislative changes to EEP. We also contacted 13 EEP exporters to obtain their perspectives and suggestions. The exporters were selected to obtain a mix of large and smaller participants in the EEP wheat, wheat flour, and vegetable oil programs. The 13 exporters we contacted received over 60 percent of the subsidies awarded under EEP for those commodities from May 1985 to May 1994. Because we judgmentally selected the exporters, their responses were not necessarily representative of all EEP exporters. Due to time constraints, we obtained the information on the EU's export subsidy system from USDA's Foreign Agricultural Service.

We did our work from May 1994 to July 1994 in accordance with generally accepted government auditing standards.

Uruguay Round Agreement Requirements

The Uruguay Round agreement, if implemented, would directly affect a number of U.S. agricultural export programs. According to FAS, the following USDA programs would be subject to the subsidy reduction requirements of the Uruguay Round agreement: EEP, the Sunflowerseed Oil Assistance Program (SOAP), the Cottonseed Oil Assistance Program (COAP), the Dairy Export Incentive Program (DEIP), and the Commodity Credit Corporation's (CCC) Direct Sales Program.[3] USDA's export credit programs, such as the General Sales Manager (GSM) 102 and 103 programs, would not be restricted by the Uruguay Round agreement. However, the member countries committed to working toward achieving internationally agreed-upon disciplines governing export credit programs. There would not be required reductions in food aid programs, such as Public Law 480, titles I-III or Food for Progress. However, the Uruguay Round agreement established conditions that food aid programs would be required to meet in order not to be considered an export subsidy. Market promotion and development programs, such as the Market Promotion Program and the Cooperator Program, would remain unaffected by the Uruguay Round agreement, unless expenditures are linked to specific sales or export performance (see app. I for further information on programs and subsidy reduction effects).

Some commodities would experience greater export subsidy reductions than others from current funding levels, because reductions would be based on average subsidy levels for 1986-90. The impact would thus be heaviest on those commodities whose subsidies have increased since the base years. For example, the U.S. export budgetary outlays for wheat/wheat flour and vegetable oils would have to be reduced by 57 percent ($482 million) and 77 percent ($47 million), respectively, from the 1991-92 levels by the year 2000. Other commodities that would experience significant reductions from current funding levels include rice, eggs, and dairy products (see app. II for further information on commodity-specific effects of the agreement).

Industry and Interest Groups' Proposed Alternatives and Suggested Changes to the Current EEP

Two organizations, World Perspectives, Inc., and the National Association of Wheat Growers, proposed specific alternatives to the existing EEP program. Both proposals would expand EEP to more export markets instead of continuing its current approach of targeting countries to which the EU has subsidized exports. The WPI proposal would also establish a number of other operational changes to EEP designed to make the program more flexible for exporters and buyers while maximizing exports with available program funds. The NAWG proposal calls for the redirection of unspent EEP funds to other USDA export programs, such as food aid programs. Both proposals fell into the category of programs that would be

[3]Under the Direct Sales Program, CCC can sell surplus CCC-owned commodities in export markets at prices lower than acquisition costs. The quantity and kind of CCC commodities available determine the level of export sales each year.

subject to the reduction requirements of the Uruguay Round agreement on the use of export subsidies (see app. III for further information on these proposals).

While not an alternative proposal to EEP, a "self-help" program proposed by the dairy industry would use a marketing board to augment USDA's export marketing activities.[4] The proposal would augment rather than replace USDA-subsidized exports under DEIP. It is unclear whether such a program would fall under the Uruguay Round agreement's subsidy restrictions. Other commodity groups have expressed an interest in using marketing boards to augment EEP program activities.

The exporters we contacted expressed varying opinions on whether changes should be made to the current EEP, assuming the Uruguay Round agreement is implemented. Many of the suggestions made were intended to improve the flexibility of the program for exporters and buyers. For example, exporters want to be able to make changes that are mutually agreed upon by the exporter and buyer, such as changes in the shipping port or product specifications, without having to obtain FAS' approval. Some exporters cited the EU's agricultural export program as an example of a more flexible export subsidy program. Other exporters suggested more fundamental changes in the program, such as using EEP funds for foreign market development rather than solely for export subsidies. The exporters were divided in their support for the WPI and NAWG proposals (see apps. IV and V for further information on the exporter's suggested improvements to EEP and the EU's agricultural export program).

We were unable to evaluate the alternative proposals and suggestions made by the exporters due to the lack of criteria concerning the role and purpose of EEP in a post-Uruguay Round agreement environment. For example, if the program is primarily a trade policy tool designed to encourage competitors such as the EU to negotiate further reductions in the use of subsidies, the targeting aspect of EEP could remain an important feature of the program. However, if the program is primarily intended to increase U.S. agricultural exports, the elimination of the targeting aspect of the program could be appropriate.

FAS officials said that EEP's objectives and its relationship to U.S. agricultural trade policy should be discussed before making significant operational changes in the program. They said that they were assessing the WPI and NAWG proposals as well as considering other options to the current EEP. They expected the position paper that they were developing to serve as the basis for continued discussions within the administration and the Congress about the implications of the Uruguay Round agreement on the future of EEP.

Agency Comments

We did not obtain written agency comments on this report. However, we discussed the contents of this report with FAS officials on June 27, 1994,

[4]Marketing boards are quasi-government agencies that control the sale and export of commodities using a pooling mechanism.

including the General Sales Manager and the Director of the Commodity Credit Corporation's Operations Division, and incorporated their comments where appropriate. FAS officials generally agreed with the contents of the report and with our observation regarding the need to assess the goals and objectives of EEP in a post-Uruguay round environment before considering alternative proposals or making significant changes to the program.

As agreed with you, unless you announce the contents of this briefing report earlier, we plan no further distribution of this report until 14 days from its issue date. At that time, we will send copies to the Secretary of Agriculture and other interested parties. Copies will be made available to others on request.

The major contributors to this briefing report are listed in appendix VI. Please contact me at (202) 512-4812 if you have any questions concerning this report.

Sincerely yours,

Allan I. Mendelowitz

Allan I. Mendelowitz, Managing Director
International Trade, Finance, and
Competitiveness

Contents

Tables

Figures

Abbreviations

CCC	Commodity Credit Corporation
COAP	Cottonseed Oil Assistance Program
DEIP	Dairy Export Incentive Program
EU	European Union
EEP	Export Enhancement Program
FAS	Foreign Agricultural Service
GATT	General Agreement on Tariffs and Trade
GSM	General Sales Manager
M.E.	milk equivalents
MPP	Market Promotion Program
NAWG	National Association of Wheat Growers
OECD	Organization for Economic Cooperation and Development
SOAP	Sunflowerseed Oil Assistance Program
USDA	U.S. Department of Agriculture
WPI	World Perspectives, Inc.

Required Reductions in U.S. Export Subsidies

Figure I.1: Required Reductions in U.S. Export Subsidies

GAO **Required Reductions in U.S. Export Subsidies**

- Budget outlays reduced 36% and quantities reduced 21% from base period (1986-90)
- Annual reductions in equal installments from 1995-2000
- Annual reductions can start from the greater of
  - base period average or
  - 1991-92 average

The Uruguay Round agreement of the General Agreement on Tariffs and Trade (GATT), signed in April 1994, would require the United States to reduce its budget outlays for export subsidies by 36 percent and its quantities of commodities receiving export subsidies by 21 percent. The export subsidy percentage reductions would be applied to the base period, which would be the average level of export subsidies from 1986 through 1990. Member nations would not be allowed to take inflation into account for budget outlay reductions.

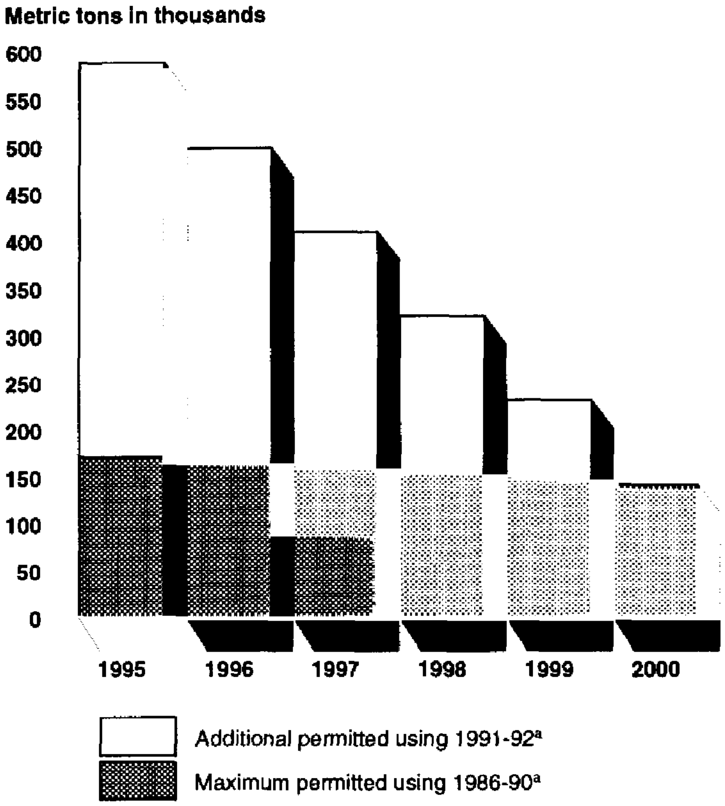
GATT member nations would be required to reduce export subsidies in equal increments on an annual basis from 1995 through the year 2000.[1] The annual percentage reductions would be 6 percent and 3.5 percent, respectively, for export subsidy budget outlays and quantities, if members began their annual reductions from the base period average. However, in cases where members' export subsidies were greater in 1991 through 1992 relative to the base period, they would be allowed, under some conditions,[2] to use the 1991 through 1992 average subsidy levels as a starting point for their export subsidy reductions.

[1]Developing countries have the flexibility to apply lower rates of reduction over a period of up to 10 years.

[2]The conditions that dictate whether member nations may begin annual export subsidy levels from 1991 through 1992 levels are contained in a GATT document entitled "Modalities for the Establishment of Specific Binding Commitments under the Reform Programme" ("modalities"), GATT Secretariat (Geneva, Switzerland: Dec. 20, 1993).

Figure I.2: Subsidized Vegetable Oil Exports Permitted With Different Starting Points

GAO Subsidized Vegetable Oil Exports Permitted with Different Starting Points



[a]Years refer to base period starting points.

Source: GAO analysis of U.S. Department of Agriculture (USDA) data.

Figure I.2 illustrates what the difference in subsidized vegetable oil exports would be by using 1991 through 1992 as a starting point for reducing subsidized exports, rather than using the 1986-90 base period as a starting point. The darker-shaded bars in figure I.2 would be the maximum level of subsidized vegetable oil exports permitted if the base period were used as a starting point. However, since subsidized vegetable oil exports were greater in 1991 through 1992 (see table II.1) than during the base period, the Uruguay Round agreement would allow the United States to begin subsidy reductions from the 1991 through 1992 levels. The lighter-shaded bars in figure I.2 would be the additional subsidized vegetable oil exports allowed by using the 1991 through 1992 levels as a starting point. Regardless of what starting point is used to reduce export subsidies, by the year 2000 the permitted subsidized vegetable oil exports would have to be reduced to the same level, which is determined relative to the 1986-90 base period. This amount is shown by the dark-shaded bar for the year 2000 in figure I.2.

Figure I.3: USDA Export Subsidy Programs Subject to Reductions

GAO **USDA Export Subsidy Programs Subject to Reductions**

- Export Enhancement Program (EEP)
- Sunflowerseed Oil Assistance Program (SOAP)
- Cottonseed Oil Assistance Program (COAP)
- Dairy Export Incentive Program (DEIP)
- Commodity Credit Corporation (CCC) Direct Sales

USDA Export Subsidy Programs Subject to Reductions

The Uruguay Round agreement would affect specific types of subsidy programs for agricultural commodities. The following subsidies would be subject to reduction under the Uruguay Round agreement:

- direct subsidies, including payments-in-kind to firms, industries, producers, and cooperatives or to a marketing board contingent on export performance;
- sale or disposal for export by governments or their agencies of noncommercial stocks of agricultural products at a price lower than the domestic price for a like product;
- payments on the export of an agricultural product financed by virtue of governmental action, including payments financed by levies imposed on the agricultural product;

- subsidies to reduce the cost of marketing exports (other than widely available export promotion and advisory servi-ces) including handling, upgrading, and other processing costs, and the costs of international transport and freight;
- internal transport and freight charges on export shipments provided by governments, on terms more favorable than for domestic shipments; and
- subsidies on agricultural products contingent on their incorporation in exported products.

According to officials from USDA's Foreign Agricultural Service (FAS), which administers the programs, EEP, SOAP, COAP, DEIP, and CCC direct sales would be subject to reduction under the Uruguay Round agreement. The EEP is by far the largest of these programs in terms of budget outlays. According to USDA's 1995 budget document, the following amounts were spent for subsidy payments on these programs during fiscal year 1993: $967.3 million on EEP; $32.1 million on SOAP and COAP;[3] and $161.8 million on DEIP.

No figures were available for CCC direct sales during fiscal year 1993 from USDA's 1995 budget document.

According to FAS officials, the previously mentioned USDA export programs, and the commodities covered by them, are reported in the aggregate in the country schedules. (See app. II for a description of "country schedules.") USDA would be responsible for working out the details on reducing the expenditure levels and quantities for these programs to ensure that the United States complied with the export subsidy reduction requirements of the Uruguay Round agreement.

[3]The administration has proposed eliminating these programs and using EEP for vegetable oils.

Figure I.4: USDA Export Programs Not Affected by the Agreement

GAO **USDA Export Programs Not Affected by the Agreement**

- CCC export credits (General Sales Manager 102 and 103 programs)
- Market Promotion Program (MPP) Cooperators, trade shows
- Food aid programs (P.L. 480- Titles I, II, & III; Food for Progress; Section 416)

USDA Export Programs Not Affected by the Agreement

According to FAS officials, the USDA programs for export credit, food aid, and market promotion, including the Market Promotion Program, would not be subject to reductions under the Uruguay Round agreement. However, the agreement has guidelines for food aid and market promotion to ensure that these programs would not be used to circumvent export subsidy reductions. Specifically, the agreement established the following guidelines for food aid to ensure that member nations would not try to avoid the export subsidy reductions:

- International food aid should not be tied directly or indirectly to commercial exports of agricultural products.

- International food aid should be carried out in accordance with the Food and Agricultural Organization's[4] "Principles of Surplus Disposal and Consultative Obligations."
- International food aid should be granted to the extent possible in full grant form.

According to FAS officials, USDA's Food Aid programs—Public Law 480 titles I, II, and III; Food for Progress; and Section 416 of the Agricultural Act of 1949 (P.L. 439, as amended)—meet the stated guidelines.

The Uruguay Round agreement also has guidelines for the use of market promotion programs. According to FAS officials, market promotion, including the Market Promotion Program, would be allowable as long as it was not used to reduce the cost of exporting the agricultural product.

In addition to guidelines for food aid and market promotion, the Uruguay Round agreement calls for member nations to meet to develop guidelines for export credits. The agreement states that member nations would work toward developing guidelines to govern the provision of export credits, export credit guarantees, and insurance programs. According to FAS officials, the Organization for Economic Cooperation and Development (OECD)[5] formed a group that will meet in December to begin discussions on agricultural export credit guidelines. FAS officials told us that OECD was chosen as the forum because the organization has developed export credit guidelines for industrial products.

[4]The Food and Agricultural Organization is a body within the United Nations to help members deal with agricultural trade issues.

[5]OECD was established in December 1960 by the United States, Canada, and some European nations to study and discuss trade and related matters. Members include the United States, Canada, the European Union, the European Free Trade Association (Austria, Finland, Iceland, Norway, Sweden, and Switzerland), Australia, New Zealand, Japan, and Turkey.

Impact of the Uruguay Round Export Subsidy Reductions on a Commodity-Specific Basis

Table II.1: U.S. Country Schedules—Quantity Commitments Under the Uruguay Round

Metric tons in thousands

	Starting point for reductions		Quantity commitments (marketing year July 1-June 30)						
Commodity	**Base (1986-90)**	**1991-92**	**1995**	**1996**	**1997**	**1998**	**1999**	**2000**	**Government programs affected**
Wheat/wheat flour	18,382	21,382	20,238	19,095	17,952	16,809	15,665	14,522	EEP
Coarse grains	1,975	N.R.	1,906	1,837	1,768	1,699	1,630	1,561	EEP
Rice	49	318	272	225	178	132	85	39	EEP
Vegetable oils	179	677	588	498	409	320	231	141	EEP, SOAP, COAP
Butter/butteroil	27	47	43	39	34	30	25	21	Direct sales, DEIP
Skim milk powder	86	116	108	100	92	84	76	68	Direct sales, DEIP
Cheese	4	4	4	4	4	3	3	3	Direct sales, DEIP
Other milk products	0.04	15	12	10	7	5	3	0.03	DEIP
Bovine meat	22	N.R.	21	21	20	19	18	18	Direct sales
Pigmeat	0.5	N.R.	0.5	0.5	0.4	0.4	0.4	0.4	Direct sales
Poultry meat	35	N.R.	34	33	32	30	29	28	EEP
Live dairy cattle (head)	13,955	N.R.	13,467	12,978	12,490	12,000	11,513	11,024	EEP
Eggs (thousand dozen)	8,759	34,930	30,262	25,593	20,925	16,256	11,588	6,920	EEP

Legend

N.R.Not reported. Values were not reported for 1991 through 1992 because these values were less than the values for the base period (1986-1990).

Source: USDA/FAS.

The export subsidy commitments that result from the Uruguay Round agreement are documented in tables known as "country schedules." The country schedules show permitted levels of export subsidy quantities and budget outlays for eligible commodity groups on an annual basis from 1995 to the year 2000 (see tables II.1 and II.2). The country schedules were subject to scrutiny by GATT members and approved by the GATT Secretariat. The country schedules for the United States become legally binding under the Uruguay Round agreement if the Congress passes

Table II.2: U.S. Country Schedules—Budget Outlay Commitments Under the Uruguay Round

Dollars in millions

	Starting point for reductions		Budget outlay commitments (fiscal year)						
Commodity	**Base (1986-90)**	**1991-92**	**1995**	**1996**	**1997**	**1998**	**1999**	**2000**	**Government programs affected**
Wheat/wheat flour	$568.5	$845.8	$765.5	$685.2	$604.8	$524.5	$444.2	$363.8	EEP
Coarse grains	72.1	N.R.	67.7	63.4	59.1	54.8	50.4	46.1	EEP
Rice	3.7	18.4	15.7	13.0	10.4	7.7	5.0	2.4	EEP
Vegetable oils	22.0	60.7	53.0	45.2	37.4	29.6	21.9	14.1	EEP, SOAP, COAP
Butter/butteroil	47.7	N.R.	44.8	41.9	39.1	36.2	33.4	30.5	Direct sales, DEIP
Skim milk powder	128.8	N.R.	121.1	113.4	105.7	97.9	90.2	82.5	Direct sales, DEIP
Cheese	5.7	N.R.	5.3	5.0	4.7	4.3	4.0	3.6	Direct sales, DEIP
Other milk products	0.03	17.2	14.4	11.5	8.6	5.8	2.9	0.021	DEIP
Bovine meat	35.7	N.R.	33.5	31.4	29.2	27.1	25.0	22.8	Direct sales
Pigmeat	0.8	N.R.	.7	0.7	0.6	0.6	0.5	0.5	Direct sales
Poultry meat	22.7	N.R.	21.4	20.0	18.6	17.3	15.9	14.6	EEP
Live dairy cattle	18.6	N.R.	17.5	16.3	15.2	14.1	13.0	11.9	EEP
Eggs	2.5	8.8	7.6	6.4	5.2	4.0	2.8	1.6	EEP
Total	**$929**	**•**	**$1,168**	**1,053**	**$939**	**$824**	**$709**	**$594**	

Legend

N.R.— Not reported. Values were not reported for 1991 through 1992 because these values were less than the values for the base period (1986-1990).

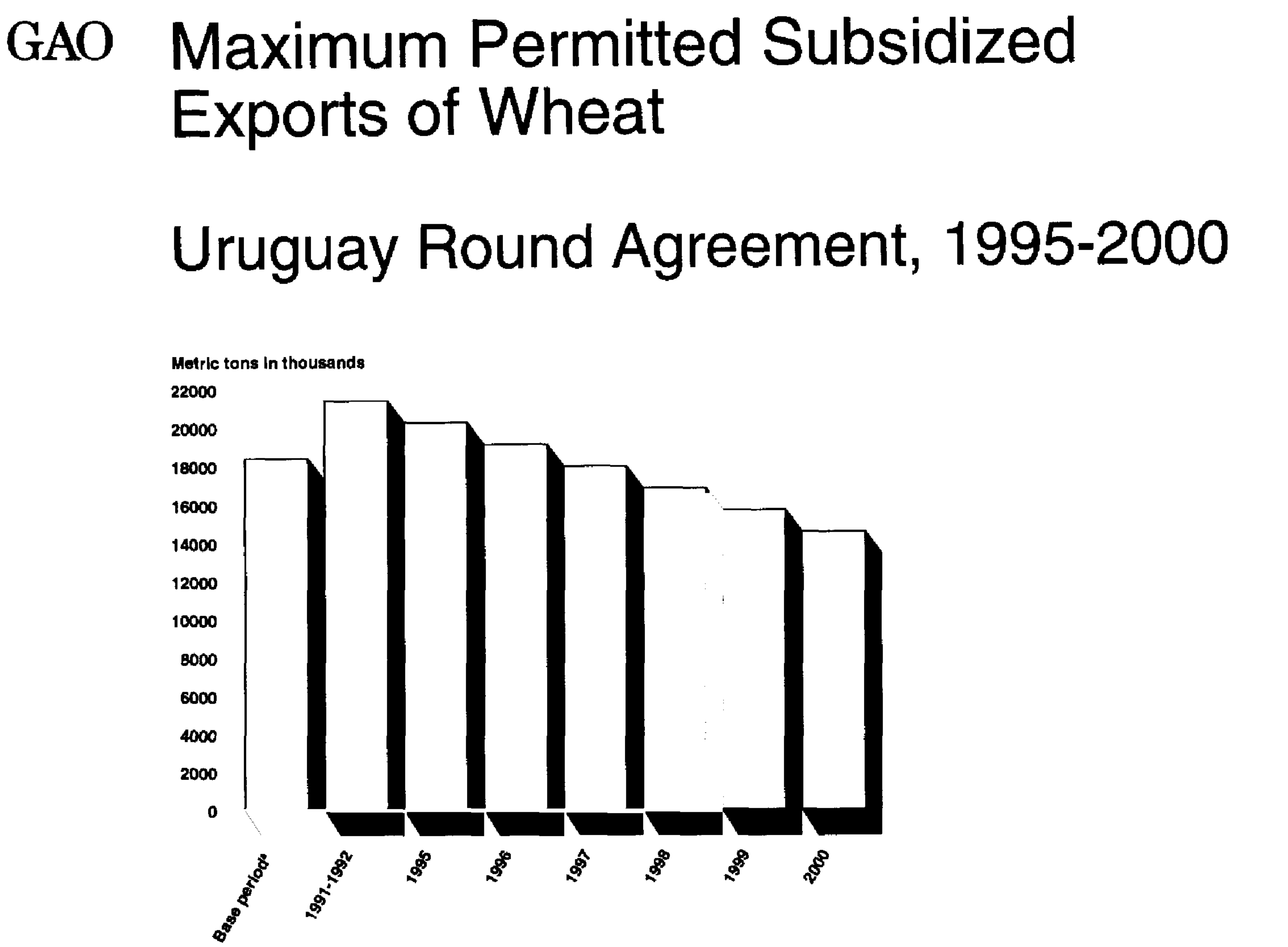
• — Could not be summed because some commodities did not report values for 1991 through 1992. However, the sum of the higher permitted starting points on a commodity specific basis equalled $1.3 billion.

Source: USDA/FAS.

implementing legislation for the Uruguay Round and the President signs it into law.

The Uruguay Round agreement would prohibit member nations from introducing or reintroducing export subsidies for products that were not subsidized during the base period. Therefore, any commodities not included in these tables could not be subsidized. According to USDA officials, some commodities in the tables are not expected to be exported under USDA export subsidy programs. These commodities were included in the tables solely to retain their eligibility for export subsidies under the Uruguay Round agreement. For example, USDA officials indicated that they had no intention of exporting live dairy cattle under any export subsidy program.

Figure II.1: Maximum Permitted Subsidized Exports of Wheat Under the Uruguay Round Agreement, 1995-2000



[a]1986 through 1990.

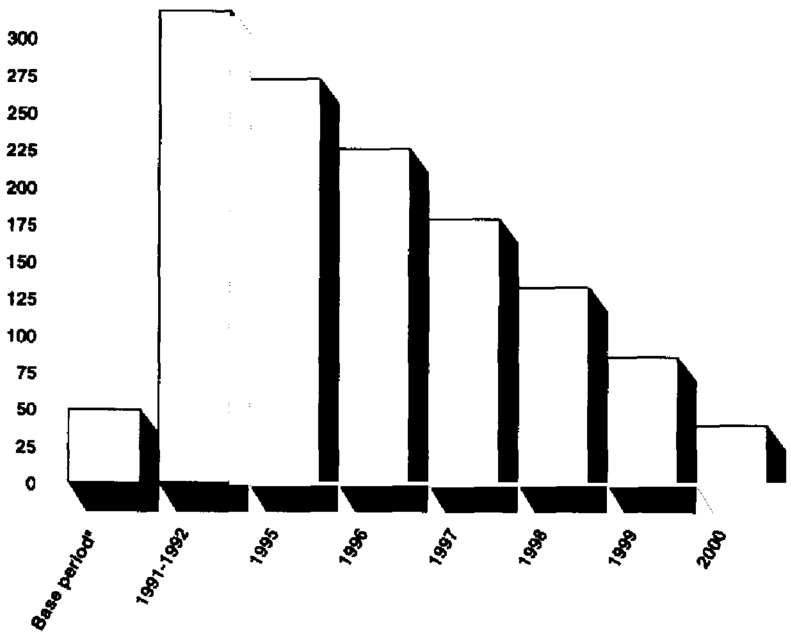
Source: GAO analysis of USDA data.

The export subsidy reductions under the Uruguay Round agreement would affect those commodities that were more heavily subsidized during 1991-92 than during the base period. Figures II.1 and II.2 show the Uruguay Round quantity reduction commitments for wheat and rice. Wheat would face a reduction of 32 percent (6.9 million metric tons) from 1991 through 1992 levels. Rice would face a greater 88-percent reduction (279,000 metric tons) from 1991 through 1992 levels.

Figure II.2: Maximum Permitted Subsidized Exports of Rice Under the Uruguay Round Agreement, 1995-2000

GAO Maximum Permitted Subsidized Exports of Rice

Uruguay Round Agreement, 1995-2000



[a]1986 through 1990.

Source: GAO analysis of USDA data.

Table II.3: Commodities With the Greatest Volume Reduction in Permitted Subsidized Exports

Metric tons in thousands

Commodity	Starting point for reductions 1991-92	Subsidy permitted in final year of implementation (2000)	Reduction from 1991-92 levels	Percentage reduction from 1991-92 levels
Other milk products	15	0.03	14.97	99.8%
Rice	318	39.00	279.00	87.7
Eggs (thousand dozen)	34,930	6,920.00	28,010	80.2
Vegetable oils	677	141.00	536.00	79.2
Wheat/wheat flour	21,382	14,522.00	6,860.00	32.1
Butter/butteroil	47	21.00	26.00	55.3
Skim milk powder	116	68.00	48.00	41.4

Source: GAO analysis of USDA/FAS data.

Tables II.3 and II.4 show the commodities that would face the largest percentage reductions from the 1991-92 averages. Table II.3 indicates that the dairy industry would face substantial percentage reductions in the quantities of permitted subsidized exports under the Uruguay Round agreement. For example, the export subsidies for other milk products (powdered milk with greater than 1.5-percent fat) would be reduced almost 100 percent.

Table II.4: Commodities With the Greatest Dollar Reductions in Permitted Subsidized Exports

Dollars in millions

Commodity	Starting point for reductions 1991-92	Subsidy permitted in final year of implementation (2000)	Reduction from 1991-92 levels	Percentage reduction from 1991-92 levels
Other milk products	$17.20	$0.02	$17.18	99.9%
Rice	18.40	2.40	16.00	87.1
Eggs (thousand dozen)	8.80	1.60	7.20	81.8
Vegetable oils	60.70	14.10	46.60	76.8
Wheat/wheat flour	845.80	363.80	482.00	57.0

Source: Analysis of USDA/FAS data.

Table II.4 shows that wheat and vegetable oils would be subject to large reductions in USDA export subsidy expenditures. Wheat expenditures would be reduced by $482 million from 1991-92 averages, while vegetable oils would face almost $47 million in expenditure reductions over the same time frame.

Organizations Proposing Changes to Subsidy Programs

Figure III.1: Organizations Proposing Changes to Subsidy Programs

GAO Organizations Proposing Changes to Subsidy Programs

- EEP alternatives:
  - World Perspectives, Inc. (WPI)
  - National Association of Wheat Growers (NAWG)
- Dairy industry "self-help" proposal

The two major proposals or alternatives to the current EEP program that we identified were from World Perspectives, Inc., (WPI) and the National Association of Wheat Growers (NAWG). WPI and NAWG developed their proposals to address the impact the Uruguay Round agreement, if implemented, would have on EEP funding levels. Both proposals would open EEP to more export markets instead of limiting EEP's targeting to those countries where the EU has subsidized exports. The WPI proposal would also establish a number of other operational changes to EEP designed to make the program more flexible for exporters and buyers. The NAWG proposal calls for the redirection of unspent EEP funds to other USDA export programs. These alternative proposals were identified during our discussions with U.S. agriculture interest groups.

We also obtained information on the dairy industry's self-help proposal. It illustrates a different option to current direct subsidy programs, such as EEP and DEIP, by emphasizing the use of marketing boards.

Figure III.2: World Perspectives, Inc.'s, Proposal

GAO World Perspectives, Inc.'s, Proposal

- Increase number of eligible countries
- Change bidding process to maximize exports
- Make bidding not contingent on existing contracts
- Increase exporter flexibility
- Penalize nonperformance

World Perspectives, Inc.'s, Proposal

World Perspectives, Inc., an agriculture and trade policy consulting firm located in Washington, D.C., has devised what it believes is a flexible, competitive subsidy system to maximize U.S. agricultural exports in world markets.[1] According to WPI, a competitive subsidy system would have the least distorting trade effect, reduce per-unit subsidies, increase the trade leverage of subsidies available, and allocate the subsidies according to real market conditions.

The WPI proposal does not present a completely detailed export subsidy system, but rather an outline for a plan to meet three U.S. policy objectives: to maximize U.S. agriculture exports, to improve EEP's cost-effectiveness, and to minimize commercial trade distortions. To meet these objectives, the WPI plan would be structured to

- eliminate the targeted allocation of subsidies by maximizing the number of countries that would be eligible to buy subsidized U.S. agricultural products;
- establish a competitive bidding process that would export the greatest volume of eligible agricultural commodities for the lowest subsidy amount;
- give exporters the flexibility to determine the timing, positioning, and destination market for export; and
- require sufficient financial performance guarantees from exporters and provide appropriate penalties for nonperformance.

Under the WPI proposal, USDA would retain administrative control of EEP to ensure consistency with annual GATT obligations to reduce export subsidies.

[1]Carol L. Brookins and Robert W. Kohlmeyer, "A WPI Alternative EEP Proposal," World Perspectives: AG Review, A Report From Washington (Washington, D.C.: Feb. 1994), pp. 22-4.

Figure III.3: National Association of Wheat Growers' Proposal

GAO

National Association of Wheat Growers' Proposal

- Focus on foreign market development and export expansion
- Remove unfair trade criteria to open EEP to all markets, eliminate targeting, and streamline operations
- Make funding available and use to full extent permitted by GATT

National Association of Wheat Growers' Proposal

The National Association of Wheat Growers has proposed amendments to EEP for inclusion in GATT implementing legislation. NAWG believes that the legislative authority for EEP should be revamped to reflect broader market development and export expansion objectives. NAWG also wants EEP to be funded at the maximum levels permitted by the Uruguay Round reduction schedule.

According to NAWG, EEP should be redefined to focus on foreign market development and export expansion objectives. One of EEP's major objectives has been to challenge unfair foreign trade practices.[2] NAWG believes that removing the unfair trade criteria would open EEP to all foreign markets, eliminate targeting, and streamline EEP operations.

NAWG also believes that EEP funding should be made available to the full extent permitted by GATT. NAWG suggests that the amount of budgetary outlays that would not be obligated due to quantity limitations under the Uruguay Round should be redirected to international food assistance programs.

The NAWG proposal is supported by a number of other commodity groups, including the American Soybean Association, the National Barley Growers Association, the National Cotton Council, the U.S. Rice Producers, and the Rice Millers Association.

[2]EEP initiatives must have the potential to further the U.S. trade policy strategy of opposing competitors' subsidies and other unfair trade practices by displacing other countries' subsidized exports in targeted countries. Targeted countries are those where U.S. sales have been nonexistent, displaced, reduced, or threatened because of competition from subsidized exports.

Figure III.4: Dairy Industry's "Self-Help" Proposal

GAO Dairy Industry's "Self-Help" Proposal

Dairy Producer Market Stabilization and Export Development Act of 1994 (H.R. 2664, as amended)

- Would create a Dairy Market Development Board financed by producers
- Would augment DEIP program
- Would penalize excess production

Dairy Industry's "Self-Help" Proposal

The Congress is considering legislation, the Dairy Producer Market Stabilization and Export Development Act of 1994 (H.R. 2664, as amended, 103rd Cong.), that would establish a dairy self-help program. A key feature of the bill would be the establishment of a Dairy Market Development Board. The board would consist of dairy producers and processors who would assist USDA with the disposal of a portion of surplus dairy products in export markets. The board would also penalize producers when surpluses are excessive. The program is intended to augment the current DEIP and extend the dairy price support program rather than replace them. The bill calls for the extension of authority for these programs through the year 2000. The bill passed the Livestock, Dairy, and Poultry Subcommittee of the House Agriculture Committee on June 8, 1994, and was reported to the full House Agriculture Committee.

The initial version of the legislation was amended to address concerns over compatibility with the Uruguay Round agreement requirements. According to FAS, it is still uncertain whether the current dairy self-help proposal and marketing boards in general would or would not be subject to the export subsidy reduction requirements contained in the Uruguay Round agreement.

Figure III.5: Proposed Dairy Market Development Board

GAO

Proposed Dairy Market Development Board

Responsibilities

- Coordinate export market expansion efforts
- Pool dairy revenues
- Dispose of production surpluses in excess of 5 billion pounds, as feasible.

Proposed Dairy Market Development Board

The proposed Dairy Market Development Board would operate under a contract with the Secretary of Agriculture to coordinate and facilitate the export of dairy products under a blend pricing (class IV) system.[3] The board would only engage in the removal of dairy products[4] once government purchases of dairy products exceeds 5 billion pounds, in milk equivalents (M.E.) each year.

According to FAS, if the board is unable to export the surplus products it purchases, USDA would remain the purchaser of last resort. If government purchases of surplus dairy products are expected to be above 7 billion pounds M.E., USDA would assess only those producers who are responsible for surplus production. Currently, all dairy farmers are assessed the full cost of making purchases over that level. The bill would target those producers who increase their monthly milk production above the level of production in the same month of the previous year. The bill would exempt from the assessment any producer who increases production as a result of increased efficiency due to modernization of his or her facility. It would also allow for a refund of the assessment if actual purchases fall short of 7 billion pounds M.E.

The Dairy Market Development Board would also be responsible for coordinating dairy industry efforts to expand export market opportunities for U.S. dairy products by facilitating export sales of those products. The board would pool dairy revenues on a nationwide basis to pay for the cost of board purchasing and export marketing activities. In order to do this, the board would authorize a class IV pricing pool. The pool would indirectly assess producers through a reduction in the price of surplus milk to be shared equally by all producers. The board would also be responsible for assuring that export sales under the plan would not replace existing export sales of U.S. dairy products under DEIP.

[3]The blend pricing (class IV) system is used to establish a fair and equitable blend price for milk used in commercially exported dairy products. A blend price is a weighted average price of the different classes (usages) of milk.

[4]Dairy products represented on the board are cheese, fluid milk, butter, nonfat dry milk, whole milk powder, yogurt, and frozen dairy products.

Exporter Suggestions on How to Improve EEP

Figure IV.1: Exporter Suggestions on How to Improve EEP

GAO **Exporter Suggestions on How to Improve EEP**

13 EEP exporters contacted

- Judgmentally selected
- Large and smaller EEP exporters for wheat, wheat flour, and vegetable oil

Trade consultants and exporter associations have raised questions about the need for and desired structure of EEP in a post-Uruguay Round agreement environment. These questions centered on the effectiveness of the current program in meeting its program objectives of (1) increasing U.S. agricultural exports and (2) functioning as a trade policy tool to get U.S. competitors to negotiate reductions of their export subsidies. To obtain different viewpoints on these questions as well as to discuss possible changes that could be made to improve this program, we contacted 13 judgmentally selected EEP exporters. We selected the exporters to include a mix of large and smaller exporters receiving EEP bonuses for wheat, wheat flour, and vegetable oil. The 13 exporters received over 75 percent of wheat, 60 percent of wheat flour, and 70 percent of vegetable oil subsidies (bonuses) awarded under EEP from May 1985 to May 1994.

During our conversations with the exporters, we asked for their views on the need for and the purpose of the program in a post-Uruguay Round environment. In addition, we obtained their positions regarding the WPI and NAWG proposed alternatives to EEP. We also asked for any suggestions they might have to improve EEP, assuming that the Uruguay Round agreement is implemented.

Figure IV.2: Exporter Views on Role of EEP, Given Uruguay Round Agreement

GAO

Exporter Views on Role of EEP, Given Uruguay Round Agreement

Most exporters said EEP still necessary

- U.S. commodities will still face subsidized competition
- EEP maintains pressure on EU to negotiate further reductions

Some exporters said EEP should be eliminated

- EEP ineffective in meeting goals
- EEP still emphasizes bulk grains

Exporter Views on Role of EEP, Given Uruguay Round Agreement

Many of the exporters that we contacted said that EEP would still be necessary in a post-Uruguay Round agreement environment. Specifically, 10 of the 13 exporters we contacted cited the continued need for a subsidy program like EEP. They explained that EEP was still necessary to counter the subsidy or unfair trade practices of U.S. competitors, and the European Union in particular.[1] However, two of the exporters we contacted said that EEP would no longer be needed since competition from subsidized exports would be greatly reduced under the Uruguay Round agreement. In addition, they questioned the effectiveness of EEP in countering the EU's subsidy practices and the program's current lack of focus on high-value agricultural commodities such as wheat flour and barley malt.

Those exporters that felt that EEP would still be needed pointed out that the Uruguay Round agreement did not eliminate the use of subsidies, but instead would legitimize their use. As a result, they said that EEP would be necessary to keep the price of U.S. agricultural commodities competitive with those from subsidizing nations. In addition, they said that if the long-term goal of the United States in multilateral negotiations is to eliminate all export subsidies, programs such as EEP would be necessary to create pressure on the EU to negotiate further reductions.

Two of the exporters we contacted said that EEP should be eliminated. They questioned whether the benefits of the program would outweigh the costs. In addition, they said that they did not see evidence that EEP has been effective in increasing U.S. agricultural exports or expanding U.S. agricultural markets. They said that EEP has not maintained pace with the world agricultural marketplace shift from a bulk commodity orientation to one favoring high-value agricultural products and commodities.[2]

---

[1]One of the 13 exporters did not clearly support or oppose the continued existence of EEP if the Uruguay Round agreement were implemented.

[2]Bulk commodities include wheat, feedgrains, and rice. High-value products include processed commodities (e.g., wheat flour, barley malt, and vegetable oils) and unprocessed products that are intrinsically higher in value (e.g., table eggs, frozen poultry, and nuts).

Figure IV.3: Exporter Support for WPI and NAWG Proposals

GAO

Exporter Support for WPI and NAWG Proposals

Divided support for proposals

- Supporters liked increasing the number of eligible countries
- Opponents said the elimination of targeting would weaken EEP's value as a trade policy tool

Exporter Support for WPI and NAWG Proposals

There was divided support on the part of exporters we contacted for the WPI and NAWG proposals discussed in appendix III. Of the 13 exporters contacted regarding the WPI proposal, 5 supported the proposal, 5 were against the proposal, 2 had mixed positions, and 1 had no position. Regarding the NAWG proposal, 4 supported the proposal, 7 were against the proposal, and 2 had no position. The largest EEP exporters were generally against the WPI and NAWG proposals, and the smaller exporters more likely to support the two proposals.

Exporters supporting the alternative proposals indicated that the proposals would allow exporters and buyers significantly more flexibility than the current program. In particular, they supported the elimination of the targeting aspect of the current EEP and allowing the program to be used in a greater number of markets.

Some of those that were against the WPI and NAWG proposals said the targeting aspect of EEP would continue to be necessary if the program is intended to encourage the EU to undertake negotiations for further subsidy reductions. One exporter who was against the alternative proposals said that the elimination of the targeting feature of the program would result in adverse effects on nonsubsidizing countries such as Canada and Argentina, because exporters would be free to use the EEP subsidy in markets in which the only competition was from nonsubsidizing countries.

Figure IV.4: Exporter Recommendations to Improve EEP

GAO

Exporter Recommendations to Improve EEP

- Make EEP more flexible
- Model EEP on the EU's export subsidy system
- Eliminate/streamline interagency approval process
- Emphasize emerging markets and high-value commodities
- Rethink agricultural trade policy

Exporter Recommendations to Improve EEP

The exporters that we contacted had a number of suggestions about how EEP could be improved. Many of the exporters said that EEP could be improved by making it more flexible and responsive to the commercial realities of the export marketplace. They explained that frequently it is necessary to change the shipping periods, ports, or commodity specifications of the initial contract agreement. Even when those changes are mutually consented to by the exporter and buyer, currently EEP requires FAS to approve the contract modifications. In addition, FAS sometimes changes the subsidy amount as a result of the modifications. Exporters also said that the EEP process for awarding subsidies is extremely frustrating for buyers since the exporters can only negotiate a tentative contract that is frequently rejected by FAS. As a result, the exporters said that buyers will do business with someone else who can make a firm contract commitment without involving a third party.

Other suggestions for improving the EEP program were to

- modify EEP to more closely resemble the EU's export subsidy program, which allows more flexibility regarding the timing, location, and ability to make contract modifications than EEP;
- eliminate or streamline the interagency approval process so that exporters can react more quickly to changing marketplace demands;
- focus the program more strategically to emphasize emerging markets, such as those in South America, and high-value commodities, such as wheat flour and barley malt; and
- publicly announce a maximum bonus amount and award subsidies based on the lowest bonus bid.

Two of the exporters said that rather than concentrate on improving EEP, the United States should rethink its agricultural trade policies and then focus on structuring the programs necessary to meet its trade policy objectives. For example, instead of having a subsidy program, the United States may want to use program funds to develop and implement market development strategies that would increase world demand for high-value commodities. This goal might be achieved by providing investment incentives to other countries to purchase agricultural processing equipment, thereby creating more demand for U.S. agricultural commodities. In addition, the United States could make creative use of the export credit program to stimulate greater demand for U.S. agricultural commodities.

European Union's Export Subsidy System

Figure V.1: European Union's Export Subsidy System

GAO European Union's Export Subsidy System

- System of price supports and import levies keeps internal prices high
- Exporters use various export subsidies to sell EU agricultural commodities at lower prices

The central feature of the EU grain regime is a price structure that keeps EU domestic prices above world market prices. The regime works primarily through a system of variable import levies and export subsidies. The variable import levies keep imports from undercutting the EU domestic prices. And, the export subsidies enable EU exports to be priced low enough to be sold in markets outside the EU.

Under the basic EU grain regime, the EU producer has three main options in marketing grain: (1) use or store the grain on the farm, (2) sell the grain to intervention agencies[1] at a guaranteed floor price, or (3) sell the grain on the domestic market at the prevailing EU market price.

Exporters of wheat in the EU can export either grain purchased from intervention stocks or from the open market. In either case, several different types of subsidies are available to lower the price of the EU grain to world market prices so that an export sale can be made.

[1]An intervention agency is a EU government agency that purchases surplus grain from producers at a guaranteed minimum price. This surplus grain is called "intervention stocks."

Figure V.2: EU Intervention Stock Sales

GAO EU Intervention Stock Sales

- Exporters bid for specific quantities of grain
  - Bids awarded on price
  - Exporters can sell the stock to any destination within eight geographic zones
- Fixed subsidy available under special circumstances to specific destinations

EU Intervention Stock Sales

Grain purchased from intervention stocks is awarded on the basis of competitive bidding in which the bids are won by the bidders offering the highest prices. In addition, under certain circumstances[2] fixed subsidies are available to exporters of intervention grain stocks going to specific destinations.

[2]The EU offers exporters a Common Right Restitution, which is a fixed subsidy. These subsidies are available only for specified quantities to specific destinations within a defined time period. These fixed subsidies are available for both intervention stocks and open market grain purchases.

Figure V.3: EU Free Market Export Subsidies

GAO

EU Free Market Export Subsidies

- Variable subsidies awarded on amount of subsidy requested
  - Low bidder wins award
- Fixed subsidies available under special circumstances to specific destinations

EU Free Market Export Subsidies

Exports of free market grain need to be subsidized in order to compete in world markets. Access to variable subsidies is made available through a competitive bidding process in which subsides for exports are awarded to bidders who make the lowest subsidy requests. In addition, under certain circumstances fixed subsidies may also be available to specific destinations.

Figure V.4: Flexibility in EU Export Subsidy System

GAO

Flexibility in EU Export Subsidy System

Subsidies are

- valid for current month plus additional 4 months
- valid for any destination within eight geographic zones
- Available for sale to one other exporter
- Made without a sales contract

Flexibility in EU Export Subsidy System

The EU system offers considerable flexibility to the exporter. The exporter has leeway to export to any country within eight specified geographic zones during a time period of up to 5 months. The exporters are not required to have a specific sales contract in order to bid on intervention stocks or to get export subsidies. Furthermore, a winning bidder may sell the right to make a subsidized export to one other party. In addition, a winning bidder may allow the right to make a subsidized export lapse; however, a performance bond will then be forfeited. In addition to these variable subsidies, there are also, under certain circumstances, subsidized export rights that may be good for as long as 2 years.

In contrast, EEP is a targeted export program that ties the subsidy to a specific country and time frame. Countries and commodities must first be approved under an interagency process before EEP subsidies can be awarded. Exporters must negotiate a specific sales contract with a buyer before they can bid on an EEP subsidy. FAS reserves the right to change or revoke the subsidy award if changes are made from the original contract specifications. Unlike the EU export subsidy system, exporters obtaining the rights to an EEP subsidy cannot sell or transfer the subsidy award to another exporter. Like the EU export subsidy system, exporters must maintain a performance bond to, among other things, guard against nonperformance of the subsidized export.

Major Contributors to This Report

General Government Division, Washington, D.C.

Phillip J. Thomas, Assistant Director
Laura C. Filipescu, Evaluator
Susan S. Westin, Senior Economist
Rona H. Mendelsohn, Evaluator (Communications Analyst)

San Francisco Regional Office

Kane A. Wong, Assistant Director
Harry Medina, Evaluator-in-Charge
Jose R. Peña, Evaluator

Philadelphia Regional Office

Douglas W. Sanner, Evaluator

Ordering Information

The first copy of each GAO report and testimony is free. Additional copies are $2 each. Orders should be sent to the following address, accompanied by a check or money order made out to the Superintendent of Documents, when necessary. Orders for 100 or more copies to be mailed to a single address are discounted 25 percent.

Orders by mail:

U.S. General Accounting Office
P.O. Box 6015
Gaithersburg, MD 20884-6015

or visit:

Room 1100
700 4th St. NW (corner of 4th and G Sts. NW)
U.S. General Accounting Office
Washington, DC

Orders may also be placed by calling (202) 512-6000 or by using fax number (301) 258-4066.

Each day, GAO issues a list of newly available reports and testimony. To receive facsimile copies of the daily list or any list from the past 30 days, please call (301) 258-4097 using a touchtone phone. A recorded menu will provide information on how to obtain these lists.

PRINTED ON RECYCLED PAPER