14○12 1

GAO

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

General Government Division

B-252686

March 18, 1993

148757

The Honorable Bob Graham
United States Senate

Dear Senator Graham:

This letter responds to your request that we review the "snapback" tariff provision for fresh fruits and vegetables (article 702) of the Canadian-U.S. Free Trade Agreement (CFTA) and the agricultural safeguard provisions between the United States and Mexico under the North American Free Trade Agreement (NAFTA).[1] Specifically, our objectives were to (1) explain the CFTA snapback mechanism and how it works; (2) discuss the NAFTA safeguard mechanism and how it fits in with the NAFTA transitional tariff system; (3) determine the criteria on which U.S. agriculture officials selected certain fruits and vegetables to be safeguarded; and (4) describe the protection that the NAFTA safeguard affords U.S. commercial fruit and vegetable growers.

SCOPE AND METHODOLOGY

To obtain data on the U.S. government's implementation of the CFTA snapback mechanism and its efficacy, we interviewed officials at the U.S. Department of Agriculture (USDA) and the U.S. Customs Service. In addition, USDA and Customs officials provided information on the process for collecting import price data needed to apply the snapback mechanism.

We obtained Canadian government data on their use of the snapback mechanism from the appropriate officials in

---

[1]The CFTA snapback tariff provision provides for conditional, temporary tariffs to protect the importing country's domestic growers of fresh fruits and vegetables against surges in unusually low-priced imports. It will expire at the end of 2008. The NAFTA safeguard mechanism also applies to fruits and vegetables but its trigger will be based upon import volume rather than price.

057545/148757

Ottawa, Canada, and from the Canadian Horticultural Council, a Canadian national trade organization. We collected data on the NAFTA safeguard mechanism from U.S. Trade Representative officials (USTR) and USDA officials. In addition, we obtained a growers' point of view on the NAFTA safeguard mechanism from the Florida Fruit and Vegetable Association and the United Fresh Fruit and Vegetable Association. We did our review between June 1992 and January 1993.

THE CFTA SNAPBACK MECHANISM

Under article 702 of CFTA, the United States and Canada agreed to maintain a conditional snapback tariff mechanism for a 20-year period to protect against unusually low-priced imports of certain fresh fruits and vegetables. The snapback may be applied when two conditions are met: (1) For each of five consecutive working days, the import price for a particular commodity is below 90 percent of the average monthly import price, for the month in which that day falls, over the preceding five years, excluding the years with the highest and lowest average monthly import price; and (2) the planted acreage for the particular fruit or vegetable in the importing country is no higher than the average acreage over the preceding five years, excluding the years with the highest and lowest acreage. The duty, or tariff, applied under the CFTA snapback provision, together with any other duty in effect for the particular fruit or vegetable, cannot exceed the lesser of (1) the most-favored-nation (MFN) tariff that was in effect for the corresponding season before CFTA was signed or (2) the MFN rate of duty in effect for that particular fresh fruit or vegetable at the time the temporary duty is applied. Tariffs on all fruits and vegetables eligible for the snapback are being phased out over ten years.

Before implementing a snapback tariff, a country must notify the targeted country and give it two working days (not including weekends or holidays) to respond. Once applied, the snapback tariff can remain in effect for a maximum of 180 days. It must be removed immediately once the producers' export price exceeds 90 percent of the 5-year average for five consecutive days. It cannot then be reapplied until the next marketing season.

How the CFTA Snapback Mechanism Works

The U.S. Customs Service's Automated Commercial System is used to collect data needed to monitor Canadian import prices. Importers/brokers enter data directly into the computerized system, including information such as tariff codes, port of entry, product name, and price. Under the Public Law 100-449, they are allowed ten working days to do so. USDA provides Customs with a list of specific tariff numbers to monitor, and Customs extracts the appropriate importer/broker data and forwards the information to USDA.

The Canadians have a similar system, but they use a survey form to collect import price information, such as tariff numbers and prices, at the border. While this system provides more timely data, U.S. Customs officials said that it is more costly than the current U.S. system. They also said that the value of the commodity may be set on a "consignment" basis (i.e., the product does not have a price when it crosses the border). The reported price, therefore, may not reflect actual market value.

Effectiveness of the CFTA Snapback Mechanism

The United States has not applied a CFTA snapback tariff since CFTA took effect in 1989 because the required conditions (price and acreage) have not been met. USDA officials said that the main reason the conditions have not been present is that, relative to U.S.-Canada trade, the United States is the predominant producer and price leader for most fresh fruits and vegetables. Canada's cold climate severely limits the variety and quantity of fresh fruits and vegetables that can be grown.Therefore, Canada is the leading importer of most U.S. fresh fruits and vegetables. In 1991, the United States shipped about $1.22 billion of these products to Canada, while Canadian shipments to the United States were valued at only $148 million.

Canada has applied the snapback mechanism five times since its passage. Prices for the produce imports from the United States were low enough to trigger the price criteria an additional five times, but the Canadian acreage criterion was not met. From 1990 to 1992, Canada applied the snapback provision to asparagus, peaches, tomatoes, cabbage, and lettuce.

Canadian growers of fruits and vegetables do not like the acreage criterion because it limits the potential use of the snapback mechanism. In addition, they say that the time required to justify the application of the snapback, combined with market price volatility, can limit the use of the snapback. It can take up to nine or ten days to meet the requirements: five consecutive days of tracking the price, two days prior notice to the trading partner, a weekend, and possibly a government holiday. Prices could plummet and then rise again by the time the 9-or 10-day time period passes.

THE NAFTA SAFEGUARD PROVISIONS FOR AGRICULTURAL PRODUCTS

The agricultural safeguard provisions in NAFTA are an integral part of the provisions for phasing out tariff protection.[2] As applied to U.S. imports from Mexico, the safeguard will pertain only to products considered as import sensitive. The safeguard, referred to as a (seasonal) tariff rate quota (TRQ), allows imports at the NAFTA preferential tariff rate up to a certain quota level. Once the import volume of a product reaches the quota level, further imports during that season will be subject to the MFN tariff rate in effect at the initiation of NAFTA, or, if lower, the MFN rate in effect when the safeguard is triggered. The quotas will grow at a 3-percent compounded annual rate. USDA officials stated that the NAFTA preferential tariff rate will be reduced by 10 percent of the base tariff each year until it is eliminated in the tenth year.

An essential difference between the NAFTA safeguard and CFTA snapback mechanisms is that the former is triggered on the basis of import volume, while the latter is triggered

[2]If ratified, the agricultural agreement in NAFTA will contain two bilateral sections governing market access, one between the United States and Mexico, and the other between Canada and Mexico. Both sections include special safeguard mechanisms for various "import sensitive" agricultural products. The CFTA rules for the elimination of tariff and nontariff barriers will continue to apply to agricultural trade between Canada and the United States, and include the snapback provision.

by import price. U.S. agriculture officials developed this strategy because many fruits and vegetables from Mexico are imported on a consignment basis. Also, Mexico does not have the complex data collecting processes in place for monitoring prices and acreage.

NAFTA provides safeguards for six U.S. products: chili peppers, eggplant, onions, squash, two seasons of tomatoes, and watermelon. NAFTA safeguards 17 Mexican products, including 11 categories of pork; frozen, fresh and dried potatoes, and potato chips; fresh apples; and extracts, essences, or concentrates of coffee. The safeguarded U.S. and Mexican products are listed in the transitional tariff schedule. According to USDA officials, TRQs assigned to these products are based on the highest levels of import volume during calendar years 1989-91 plus 5 percent. The NAFTA preferential tariff rate, based on either volume or value, applies up to the specified import quota level.

The enclosure lists selected fruit and vegetable products and their associated import seasons, safeguard quotas (TRQs), NAFTA preferential tariff rates, and phase-out periods for those tariffs.

NAFTA Transitional Tariff System

The NAFTA transitional tariff system has been set up for all agricultural products in both of the bilateral agreements. There are nine categories of transitional tariffs. However, fresh fruits and vegetables and other horticultural products fit into only five of these categories of transitional tariffs, each having a different phase-out period according to the level of import sensitivity of the product. A description of the transitional tariff categories, including the category of safeguarded products, follows:

1. Category A - Immediate elimination of all tariffs. The tariffs on these products are generally low enough that the products are not considered to be import sensitive.

2. Category B - Medium-term phase-out of five years in equal increments.

3. Category C - Long-term phase-out of ten years. These products are considered import sensitive. Again, phase-out will be in equal increments.

4. Category C+TRQ (safeguarded products) - Highly import sensitive U.S. commodity with a tariff-rate quota and a phase-out period of 10 years.

5. Category C+ - Extra-long-term phase-out period of 15 years.

In addition to the fresh fruit and vegetable categories above, some other products have a 15-year transition period and a TRQ. Frozen orange juice concentrate and single strength orange juice (not concentrated) both have a 15-year transition period, with an non-linear tariff phase-out, and a TRQ. Along with peanuts and sugar, these commodities are considered to be very import sensitive and, as a result, were given the longest transition period to adjust to NAFTA market conditions.

CRITERIA ON WHICH NAFTA SAFEGUARDED PRODUCTS WERE SELECTED

U.S. agricultural officials used information from a variety of sources to determine which fruits and vegetables were more import sensitive than others. For example, in the case of tomatoes, USDA officials said that both the Agricultural Technical Advisory Committee (ATAC) and Agricultural Policy Advisory Committee (APAC) were solicited for their views on each tariff offer during the negotiations for NAFTA.[3] They said that the committees sat down with USDA officials and went through the tariff schedules line by line. In addition, USDA officials solicited individual growers, consumers, and processors for their views. USDA officials told us that they attempted to balance the divergent interests of those solicited.

[3]ATAC and APAC for Trade in Fruits and Vegetables are legislatively established private sector advisory committees that report to the Secretary of Agriculture and the U.S. Trade Representative. As required by the Trade Act of 1974, as amended, 19 U.S.C.-2155 (e), they prepared reports to summarize the views of their members regarding the impact of NAFTA on the industries they represent.

According to USDA officials, the tariff phase-out periods were, to some extent, based on the current tariff on each product. For example, they said that the relatively low tariff rates of 3.3 cents and 4.6 cents per kilogram on tomatoes were not providing much protection. Therefore, tariffs on tomatoes were given a short phase-out period. On the other hand, orange juice, with its current tariff of 9.25 cents per liter, is considered a "super import sensitive" product. Similarly, sugar and peanuts, imports which are restricted under Section 22 of the Agricultural Adjustment Act of 1937, are considered to be in the most import sensitive category. Consequently, they have the longest transition period.

PROTECTION AFFORDED U.S. GROWERS BY NAFTA SAFEGUARD

The protection afforded U.S. growers of NAFTA-safeguarded commodities is difficult to measure. The NAFTA safeguard mechanism was not intended to permanently protect U.S. growers of certain fruits and vegetables. Rather, it provides an adjustment period to allow those farmers whose products are in direct competition with Mexican products either to develop new ways to compete or to phase into other crops. Because of its warmer climate, Mexico will continue to have a comparative advantage over the United States in producing various fruits and vegetables during the winter months. Also, because of its considerably cheaper cost of labor, Mexico continues to have an advantage in some commodities, such as asparagus and strawberries, which require highly labor-intensive harvesting.

Please contact me at (202) 512-4812 if you or your staff have any questions concerning this letter. The information in this letter was developed by Curtis F. Turnbow, Assistant Director, Lloyd K. Lindland, Evaluator-in-Charge, and Jane-Yu Li, Economic Adviser.

Sincerely yours,

Allan I. Mendelowitz

Allan I. Mendelowitz, Director
Financial Institutions and International Trade

NAFTA TARIFF SCHEDULE FOR
SELECTED FRUITS AND VEGETABLES

Product	Dates of seasonal tariff	Initial NAFTA tariff rate[a]	Safeguard quota (MTON)	Phase-out period
Tomatoes	Mar 1-Jul 14	4.6 c/kg	165,500	10 years
	Jul 15-Aug 31	3.3 c/kg	None	5 years
	Sep 1-Nov 14	4.6 c/kg	None	5 years
	Nov 15-Feb/last day	3.3 c/kg	172,300	10 years
Onions	Jan 1-Apr 30	3.9 c/kg	130,700	10 years
	May 1-Dec 31	3.9 c/kg	None	10 years
Cucumbers	Dec 1-Feb/last day	4.9 c/kg	None	Immediate
	Mar 1-May 31	6.6 c/kg	None	15 years
	Jun 1-Jun 30	6.6 c/kg	None	5 years
	Jul 1-Aug 31	3.3 c/kg	None	Immediate
	Sep 1-Sep 30	6.6 c/kg	None	5 years
	Oct 1-Nov 30	6.6 c/kg	None	15 years
Asparagus	Sep 15-Nov 15	5 %	None	Immediate (SBA)
	Jan 1-Jan 31	25%	None	Immediate to 17.5%, 15 years to 0%
	Feb 1-Jun 30	25%	None	15 years
	Jul 1-Dec 31	25%	None	5 years
Eggplant	Dec 1-Mar 31	2.4 c/kg	None	Immediate
	Apr 1-Jun 30	3.3 c/kg	3,700	10 years
	Jul 1-Sep 30	3.3 c/kg	None	Immediate
	Oct 1-Nov 30	3.3 c/kg	None	10 years

Product	Dates of seasonal tariff	Initial NAFTA tariff rate[a]	Safeguard quota (MTON)	Phase-out period
Capsicum (Bell) peppers	Nov 1-May 31	5.5 c/kg	None	10 years
	Jun 1-Oct 31	5.5 c/kg	None	5 years
Chili peppers	Oct 1-Jul 31	5.5 c/kg	29,900	10 years
	Aug 1-Sep 30	5.5 c/kg	None	Immediate
Squash	Oct 1-Jun 30	2.4 c/kg	120,800	10 years
	Jul 1-Sep 30	2.4 c/kg	None	5 years
Olives (fresh)	All Seasons	11 c/kg	None	Immediate
Oranges	Dec 1-May 31	2.2 c/kg	None	5 years
	Jun 1-Nov 30	2.2 c/kg	None	Immediate
Limes	All Seasons	2.2 c/kg	None	10 years
Cantaloupes	Jan 1-May 15[b]	Free	None	N/A
	May 16-Jul 31	35%	None	15 years
	Aug 1-Sep 15	20%	None	10 years
	Sep 16-Nov 30	35%	None	15 years
	Dec 1-Dec 31	35%	None	Immediate
Watermelons	Dec 1-Mar 31	20%	None	Immediate
	Apr 1-Apr 30	20%	None	Immediate
	May 1-Sep 30	20%	54,400	10 years
	Oct 1-Nov 30	20%	None	Immediate
Strawberries (fresh)	Jun 15-Sep 15	0.4 c/kg	None	Immediate
	Sep 16-Jun 14	1.7 c/kg	None	Immediate

[a]This column represents the initial NAFTA tariff rate from which the tariff phase-out is made and is therefore listed as the "existing U.S. tariff" -- either a specific duty (c/kg.), or an ad-valorem duty (percent).

[b]For cantaloupes during the January 1-May 15 season, no duty or tariff exists. Therefore, a phase-out period is not applicable.

Legend

c/kg = cents/kilogram

MTON = Metric tons

Safeguard Quota = Tariff rate quota

SBA = Ship by air. The 5 percent ad-valorem tariff on asparagus that is shipped by air during the period September 15-November 15 will be removed immediately.

(280022)