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New Direction for the Improvements of Special Safeguard for Developing Countries

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ABSTRACT

During the ongoing agricultural negotiations in the WTO, there have been numerous proposals for an agricultural safeguard mechanism to be provided to developing countries as a special and differential treatment measures. This study provides some detailed consideration of the design of such an instrument, focusing on a mechanism to protect small farmers from the damaging effects of temporary fluctuations in the price and quantity of imported staple food that is sensitive from a food security perspective.

I. Introduction

In the ongoing negotiations on agriculture in the WTO, many member countries, particularly developing countries have put forward proposals for an agricultural safeguard mechanism to be provided to developing countries as a special and differential treatment (S&D)in a revised URAA (Uruguay Round Agreement on Agriculture). Existing proposals are fairly general and a recent study by Ruffer, Jones, and Akroyd (2002) on S&D states that:

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"Further consideration of the design of such a safeguard is necessary to ensure that the process of invoking it is made relatively simple and that it does not entail a lengthy and costly administrative process that would be beyond the means of many developing counties."

In the September 2002 Special Session of the Committee on Agriculture, Members considered in more detail the market access proposals and by 31 March must agree on modalities for the final stage of the negotiations which must be concluded by 1 January 2005. This paper provides some detailed consideration of the design of a special agricultural safeguard mechanism (SASM) for developing countries, in particular, food-importing developing countries. The objective of SASM would be to provide developing country governments with an instrument to protect poor farmers from the damaging effects of temporary fluctuations in the price or quantities of imported staple food and other crops which are sensitive from a food security perspective.

Section 2 of the paper outlines the justifications for a SASM. Section 3 reviews existing trade defense mechanisms in the WTO agreements. Some recommendations for the design of the SASM are provided in Section 4 and the paper is concluded in Section 5.

II. Justifications for an SASG

There are several reasons for necessity of new SASM. First, there exists imbalance in current rules. Under WTO disciplines, tariffs often are only border measure that importing countries can use. With limited affordable safety-net measures available to governments and fiscal constraints limiting the choice of other domestic policy measures, it is often tariffs that are varied to safeguard farmers' interests in the face of swings in world market prices or import surges. Very few developing countries are able to use the Special Safeguard (SSG) under the URAA, which provides those that can use it with ability to levy additional duties when imports are priced below a certain reference level or in the case of a surge of imports above a specified level. Because it is mainly developed countries that are able to use the SSG, there is a perception among some member countries that is an imbalance in current rules that needs to be readdressed.

Although, the WTO agreements provided a variety of other trade defense mechanisms, few developing countries pose the legal and institutional capacity required to invoke them. It is important that such capacity is developed, but it is also important that new instruments are designed and that are relatively simple to implement by developing countries, while avoiding abuse by vested interest groups. Furthermore, the majority of WTO trade defense instruments were designed to protect industrial interests and as such do not take into account some of the peculiarities of the agricultural sector.

Second, small farmers in developing countries are vulnerable to temporary fluctuations in market conditions. They often do not have access to insurance mechanisms and safety nets because governments lack resources to make transfers to farmers and other affected groups in time of low prices. Furthermore, developing countries lack effective market based risk management tools and public institutions to deal with price risk situations.

Poor farmers' livelihoods are often extremely vulnerable and, particularly in the short term, they often lack access to income sources other than those upon which they have traditionally depended, meaning that temporary shocks can have significant negative effects on the poor. Vulnerability to external shocks is of particular concern to developing countries that are endeavoring to develop their agricultural potential and diversify production in order to enhance their food security and alleviate poverty.

Third, agricultural markets are by their nature cyclical and subject to turbulence due to weather variability, the low elasticity of demand for agricultural products, the subsidizing of agricultural production and exports, as well as the behavior of trading firms (both state-owned and private) which affect the development of and flow of trade. As countries reduce their trade barriers and bind them at lower level in the WTO, they become increasingly vulnerable to external agricultural market instability and to import surges that could be harmful to domestic producers. There are several recorded instances of market openings associated with an increased frequency of import surges which have damaged or threaten to destroy viable domestic production.[2] Although this market opening may not have always been due to commitments under the WTO, such vulnerability could increase in some instances as countries reduce tariffs and bind them at low levels. As quantitative restrictions have been replaced with tariffs, depressed prices and/or import surges have increasingly become the key external risks to the stability of domestic markets.

Sharma (2002) discusses how for basic foods, tariffs are often higher than the average rate and in many instances have been supplemented by additional measures such as surcharges and variants of price band policies. Such additional measures are often seen as necessary by developing country governments where these commodities play an important role in their economies and where small farmers' food and livelihood security is affected by trade policies for these products and where they do not have recourse to an adequate safeguard mechanism under the URAA. Sharma states that:

There are many cases of countries facing difficulties in 'living with' ordinary customs duties, notably for basic foods. This problem is of such a magnitude that it should not be ignored.

Ⅲ. Review of Existing Safeguard Mechanisms

There are a number of safeguard and trade defense measures in the WTO framework that allow for Members to temporarily suspend their obligations or provide them with additional trade

[2] For example, Jamaica has experienced import surges in meat products and sugar, which is reflected in high tariff bindings for these products. See FAO (2000).

instruments to defend domestic producers from unfair competition, transitional adjustment problems or temporary market fluctuations. These instruments were designed to address the problems that increases in imports may create for domestic producers. There is considerable debate in the WTO regarding the extent to which some of these instruments are abused. However their overall purpose is to protect domestic markets from either short term difficulties as a result of exposure to international markets or against uncompetitive or unfair practices that could cause injury to domestic producers. This section reviews the extent to which these trade measures provide adequate defense for poor farmers in developing countries and considers what lessons can be drawn in designing a SGM.

1. Agreement on Safeguard (Article XIX of the GATT, the Agreement on Safeguard)

The Agreement on Safeguards expands on and clarifies Article XIX of the GATT, which authorizes importing countries to restrict imports for temporary periods if, after investigations carried out by competent authorities, it is established that imports are taking place in such increased quantities (either absolute or in relation to domestic production) as to cause serious injury to a domestic industry that produces like or directly competitive products. If further provides that such measures, which could take the form of an increase in tariffs over bound rates or the imposition of quantity restrictions, should be applied on a non-discriminatory basis to all imports from all sources. Where a quantitative restriction is used, quota may be allocated among the main supplying countries. In such cases, individual shares are allocated in consultation with the supplying countries on the basis of their historical shares in imports. Investigations can be initiated either by government itself or on the basis of a petition from the affected industry. The Agreement lays down the criteria which investigating authorities must consider in determining whether increased imports are causing serious injury to the domestic industry. It also sets out basic procedural requirements for the conduct of the investigations.

The primary purpose of providing such temporary increased protection is to give the affected industry time to prepare itself for the increased competition that it will have to face after trade restrictions are reduced or removed. The Agreement seeks to ensure that such restrictions are applied only for temporary periods by setting a maximum period of eight years for the application of a measure on a particular product.[3]

A member proposing to apply safeguard measures is expected to offer trade compensation to countries whose trade interests would be adversely affected by such measures. If agreement on adequate trade compensation cannot be reached, the affected countries may take retaliatory action, normally in the form of suspension of a concession or other obligation to which the country applying the safeguard measure is entitled

Action under this agreement has rarely been taken by developing countries as few possess the resources and the institutional and legal capacity required to determine and prove serious injury. It is normally the industry in question that raises concerns with their government and this marks the first step of initiating the investigation. Small farmers in developing countries are unlikely to have the collective voice and resources necessary to lobby the government in this way. Also these investigations are likely to take a considerable amount of time. Such time delays could potentially mean that the action, when finally taken, is too late to protect the livelihoods of poor farmers. Furthermore the costs of compensation that must be provided to avoid retaliation by those countries whose trade interests have been adversely affected would be prohibitive in many cases. An added constraint on the use of this mechanism by developing countries is that the use of general safeguards requires that they are implemented through Members' national legislation which has not been enacted in many developing countries.

[3] Developing countries can impose them for a maximum period of ten years.

2. Special Safeguard (Article 5 of the URAA)

Article 5 of the URAA is an exception to the general rule in Article 4 prohibiting the use of border measures other than bound tariffs. The SSG applies to products that underwent tariffication during the Uruguay Round. It was created to address concerns that removing non-tariff measures might either result in a flood of imports that would hurt domestic production or depress domestic prices because duties bound through the tariffication process alone might not be sufficient. This agricultural specific instrument was seen as necessary recognizing that the general safeguard provision of the GATT was inadequate in offering the assurance required by countries undergoing a transition to a tariff-only trade regime with commitments to reduce the level of these tariffs. As many developing countries did not tariffy, offering ceiling bindings instead, few of them have access to this instrument.

Under the SSG, there are two situations when a safeguard action is authorized: a surge in the volume of imports or a sharp fall in import prices. Quantity and price triggers are defined in the URAA. Where these triggers are met, additional duties may be levied above the bound ceiling level, although safeguards under the two triggers may not be invoked concurrently.

The triggers for the imposition of the SSG are complex. They are defined as follows:

Volume-based SSG

The trigger volume is derived from[4]

(i) The actual imports over the preceding three years

(ii) The share of imports in domestic consumption over the same period

(iii) The absolute volume change in consumption over the most recent year for which data are available

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[4] See Annex 1 for a more detailed outline of the workings of the volume-based SSG.

The trigger level is higher the greatest the three-year average level of imports, the lower the share of imports in domestic consumption and the faster the growth in domestic consumption. The maximum extra duty may not exceed 30% of the ordinary level of duty in effect during the year in which the SSG is invoked. It may not be levied beyond the end of the year in which it has been imposed and it cannot be applied to imports taking place within TRQs.

Price-based SSG[5]

This must be levied on a shipment-by-shipment basis. The trigger price is defined as the average unit value of the c.i.f. price during the 1986-88 base period, expressed in domestic currency (countries using the SSG provision have notified these trigger prices to the WTO). The permitted level of the additional duty depends on the degree to which the import price falls below this trigger level. The greater the decline in the import price below the trigger level, the higher the duty in a way, the safeguard therefore works like a variable levy. However the additional duty does not completely offset the fall in the import price.

The nature of the SSG, which was intended to remain in force for the duration of the reform process, is uncertain. In the current negotiations, some members have called for its elimination, while others have proposed its continuation in a modified form, which might include extending the country and product coverage of its application.

A Background Paper by the WTO Secretariat (WTO 2002) indicates that of the 39 Members that have recourse to the SSG, ten members notified the WTO that they had taken action under the SSG from 1995-2001. For those members that invoked the SSG, it was invoked on a very small proportion of the product lines for which its use had been reserved. Table 1 shows the number of actions taken under the price and volume triggers

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[5] See Annex 2 for a more detailed outline of the workings of the price-based SSG.

TABLE 1. Number of Actions under the SSG: 1995-99

	Price-based action	Volume-based action
1995	42	5
1996	71	108
1997	96	55
1998	98	39
1999	180	31
Total	487	238

Source: WTO Secretariat.

from 1995-99. It shows that over twice as many price-based actions were invoked as volume-based actions during the period. Although the SSG is designed to be temporary in nature, some Members have continued to impose the SSG on specific products since its inception[6]

3. Lessons and Implications for an SASG

Several lessons can be learned from this review of safeguard measures currently available within WTO rules and applied in considering the design of an SASG:

Avoid requirement for proof of injury

One of the main constraints for developing countries in using existing safeguard instruments is the lengthy and costly legal and administrative procedures that accompany proof of injury. Such proof would be particularly difficult for the intended beneficiaries of the SSM. Low income and resource poor farmers are often a disparate group with little collective voice and extremely limited recourse to formal legal mechanisms and capacity to lobby government for the imposition of such safeguards.

[6] For example, the EU has maintained price-based SSGs on several sugar products every year since 1995.

Short time limits for SASG instrument

The time limits for invoking existing trade defense mechanisms vary. Given that the objective of the SASG should be to protect farmers from short term fluctuations in world markets, the use of the instrument should be limited to relatively short periods of time.

No compensation

The requirement that countries which invoke measures under the Agreement on Safeguards should provide compensation to countries adversely affected has acted as a constraint on its use by developing countries. It is therefore desirable that the SSM does not impose such a requirement.

Ⅳ. Design of New Safeguard Mechanism

The design of new SASG must be closely in line with its purpose, which is to allow countries to raise their applied tariffs above the bound ceilings in cases where, even if the ceiling was applied, domestic producers would face injury. Consequently the SASG might need to be limited in response of its breadth of coverage and depth (i.e. in terms of additional duties required). Although of benefit to farmers, in considering the design of safeguard instruments, it must be remembered that they will cost consumers of that product or those that use the product as an input into production.

There are many appealing characteristics of the existing SSG that should be adopted for the SASG. These include the following:

(i) It is relatively easy to invoke and is not particularly burdensome in its application.
(ii) It is invoked in reaction to exceptional market conditions.
(iii) It avoids requirements for proof of injury.
(iv) Measures taken are temporary in nature.
(v) It is only applicable to selected products or tariff lines.

In terms of the legal text of the URAA, there are questions over whether the SASG should be linked to the SASG as an extension to Article 5. Whether or not this would be viable, or whether a completely new article could better serve this purpose will depend on the degree of similarity between the SASG finally agreed and the existing SSG in a new URAA.

On the other hand, it could be argued that it would be better to have two independent mechanisms, since they have a different background and objectives. Furthermore, the greater vulnerability of poor farmers in developing countries and the constraints to governments to effectively support them in other ways are arguments to justify a provision that is separate to Article 5.

1. Country Coverage

It is likely that there will be a trade-off between the number of countries that are able to apply the SASG and the generosity provided in terms of the measures that can be invoked and the range of crops on which it can be applied. For the new SSM to be a meaningful mechanism for the most vulnerable countries, it may therefore be necessary for it to be limited in terms of country coverage beyond the developing countries.

However, making an objective assessment of which countries might have access to the SASG is extremely difficult. Nearly all developing country members of the WTO have significant populations of poor and food insecure people. And defining a list of food insecure countries will very much depend on the criteria used to define them.

One method of deciding on beneficiaries would relate to a country's possibilities of supporting domestic producers through government transfers. In order to differentiate between those countries that have other means to support farmers in times of low prices, access to the SASG could be limited to those countries where total domestic support does not exceed a specified proportion of the value of domestic production. The main drawback of this option is that domestic support measures will not always be a good substitute for the type of protection that the SASG is intended to provide.

An alternative method would be for the SASG to be only available to developing countries whose agricultural exports as a proportion of GDP are below a specified threshold. The inference of this is that countries are able to export large levels are unlikely to be food insecure. However, it is still difficult to see such a correlation countries with more open economies are likely to be ones who are most vulnerable to fluctuations in world markets and might therefore be the countries that would be most needy of a SASG.

2. Product Coverage

The SASG should be available for specified crops. Most proposals for the creation of a safeguard suggest that its use be restricted to a limited number of food security crops. There are several options for how they might be defined in practice:

(i) Members would report a list of food security crops in their schedules. There could be a requirement that each crop on this list is compliant with a definition stated in the URAA. Each developing country will ultimately have its own list of products related to food security. Compliance with such definition would be likely to be open to imaginative interpretation. The number of crops that each country was able to apply to the SSG list might therefore have to be limited

(ii) The broader role of particular crops for the livelihoods of many poor people in developing countries should be taken into account.

(iii) The criteria to be used in the identification of eligible products could be based on factors such as the products which contribute to the food and nutrition security status of developing countries and the role which the particular products plays in rural economy measured as a specified percentage of rural GDP. Certain thresholds could be defined for each of these factors.

3. Triggers

For the reasons already outlined, it is important that the process of invoking an SASG is relatively simple and transparent and does not entail a lengthy and costly administrative process. Triggers must be designed in such a way that recourse to the mechanism is not overly frequent. Its use must be also temporary in nature to ensure that it is used in reaction to exceptional fluctuations in world markets, rather than long term trends in commodity prices, in which case price changes should be transmitted onto the domestic market.

This means that conditions required to trigger the use of the safeguard should avoid a need for proof of injury. It would therefore be logical for the triggers for invoking the SASG to be similar to the current SSG, meaning it can be invoked when imports are priced below a certain trigger level or in case of a surge in the volume of imports above a predetermined trigger.

The validity of a price trigger is clear. Temporary fluctuations in import prices have the potential to undermine the livelihoods of small farmers and a price trigger would react to such fluctuations. The validity of a volume trigger is more ambiguous. In theory, an increase in world supply of a basic agricultural commodity will lead to a fall in its price. Such a dynamic would therefore set off the price trigger, meaning that there would be no requirement for the volume trigger. However, this assumes competitive markets. Where markets are perfectly competitive, for example in the presence of monopolistic traders, much of the fall in price caused by an increase in world supply, may be absorbed by these traders. A rapid increase in imports of a good that is not accompanied by a fall in import price would be normally be in reaction to an increase in domestic demand for that good and may not directly effect the competitive position of domestic producers. Invoking a volume trigger in this case would be likely to hurt domestic consumers. If a volume trigger is used, it is therefore important that it takes into account changes in domestic consumption levels, as is the case with the volume trigger under SSG.

Volume Trigger

Annex 1 outlines the working of the volume trigger under the SSG. The greater the share of imports in domestic consumption in the past three years, the lower the trigger level. The trigger is based on a combination of the average level of imports over the past three years and the annual change in domestic consumption in the most recent year for which data available.[7]

Ideally, the volume trigger under the SASG would work similarly, though values of the base trigger level (*X*) might be different. However, requirements for reliable and regularly updated data on domestic consumption levels for some crops may be too arduous for some developing countries. That is a real concern, particularly for the least developed countries (*LDCs*), and could make it difficult for some governments to invoke the safeguard under the volume trigger. Therefore, for the LDCs, the volume trigger should be invoked simply where the absolute volume of imports (*M*) exceeds the sum of the base trigger level (*X*) multiplied by the average quantity of imports during the three preceding years for which data are available (*MAV*). The trigger level of imports (*M*) would be therefore be defined as follows:

$$M = MAV \times X$$

Although recent and regularly updated domestic consumption levels amy not always be available, it should be possible to ascertain 'normal' domestic consumption levels based on historical data. Where this is case, the value of X should be calculated based on the share of imports in domestic consumption (S) in a 'normal year'.

7 This is intended to a account for situations where rapid increases in import levels are purely in reaction to increases in domestic demand.

Price Trigger

To avoid excessive interference with world markets, the trigger price should be set at a level that is sufficiently low so as to only offer protection in exceptional circumstances that threaten to cause injury to domestic producers. In addition, there is need for periodic adjustment to the price triggers to reflect long-term trends in commodity prices and to allow a reasonable degree of transmission of world price changes to the domestic market.

Annex 2 outlines the workings of the price trigger under the SSG. The price trigger may be imposed on a shipment-by-shipment basis where the c.i.f. import price falls more than 10 percent below a 1986-88 reference price.

The trigger under the SASG should follow a similar formula. As with the SSG, the SASG price trigger should be invoked on average price levels over a reference period (which should be periodically adjusted to take account of exchange rate fluctuations), and subject to periodic reviews. An alternative would be for Members to be given the option of choosing which of these methodologies to use, so long as the triggers are transparently reported in the WTO.

4. Safeguard Measures

The measures taken when a safeguard is invoked could take the form of an ad valorem duty or a quantitative restriction. However, as outlined in Ruffer, Jones and Akroyd (2002), there are several problems with enabling the use of quantitative restrictions (QRs):

(i) This would be inconsistent with efforts to remove QRs as part of the reform process under the URAA

(ii) QRs would imply a need to discriminate between suppliers

(iii) Tariff safeguards would be easier to manage. QRs are often administratively burdensome and expensive to maintain. Using QRs under the volume trigger would essentially mean that they were synonymous with the existing TRQ system.

Action under the SASG should therefore be limited to an ad valorem duties. For the volume trigger, these should be leveled on a non-discriminatory basis. For the price trigger, they should be leveled on a shipment-by-shipment basis. As with the SSG, the mechanism should not fully isolate domestic markets from changes in import prices.

5. Timescale

Safeguard should not be used isolate farmers from long term changes in the price of agricultural goods. They should be designed to ensure that their use is restricted to temporary changes in market conditions.

There must therefore be a limit to the time during which the SASG can be invoked. The safeguard under the price trigger should be applied on a shipment-by-shipment basis. Under the volume trigger, the imposition of the safeguard should be limited to one year, or alternatively, as is the case with the SSG, should be only maintained until the end of the calendar year in which it has been imposed

If the conditions required to invoke the safeguard continue after the end of the time limit, countries should be able to re-invoke the safeguard, through there could be limits on the number of times that a safeguard can be re-invoked. This would depend on how the reference price is calculated.

If the reference price is based on an average price during a set time period (as is the case with the SSG), then there should be a clause that limits the number of times the SASG can be re-invoked. Where this is case, repeated use of the safeguard should be limited to three consecutive crop years. This would help to ensure that the safeguard is used to help countries adjust to temporary fluctuations in market conditions as opposed to long term trends in world commodity markets. If the reference price is based on a rolling average, then, there would be apparent in changes in the average over times.

V. Conclusions

This study has argued that there is strong justification for a SASG to be provided to developing countries as a S&D measure in a revised URAA. Its design should ensure that the safeguard is relatively easy to invoke, yet is not subject to abuse. Several recommended direction for the design of new SSM is provided.

Although a SASG will be an important instrument for developing countries to enable them to insulate poor farmers from the damaging effects of temporary fluctuations in world markets, it is not the only S&D measure that is justified in a revised URAA. A recent report by Ruffer et al (2002) outlines other S&D measures that should be provided. The SASG should be provided in an environment where tariff bindings continue to be reduced, through developing countries should retain the flexibility for tariff reduction commitments on food security crops to be more gradual than average reduction commitments.

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Annex 1. The SSG Volume Trigger

Under Paragraph 4 of Article 5 of the URAA, safeguard action under the SSG may be taken under the quantitative trigger, depending on market access opportunities as follows:

Where the absolute volume of imports (M) exceeds the sum of the base trigger level (X) multiplied by the average quantity of imports during the three preceding years for which data are available (MAV) and the absolute volume change in domestic consumption of the product concerned in most recent year for which data are available compared to the preceding year (Y). i.e. the trigger level of imports (MT) is defined as follows:

$$MT = MAV \times \mathrm{X} + Y$$

The value of X is calculated based on the share of imports in domestic consumption during the three preceding years (S) as follows.

If	$S \leq 10\%$	then $X = 125\%$
	$10\% \leq \mathrm{S} \leq 10\%$	then $X = 110\%$
	$S \geq 30\%$	then $X = 105\%$

Any additional duty imposed under the quantitative trigger shall only be maintained until the end of the year in which it has been imposed and may only be levied at a level which shall not exceed one third of the level of the ordinary customs duty in effect in the year in which the action is taken.

Annex 2. The SSG Price Trigger

Under Paragraph 5 of Article 5 of the URAA, safeguard action may be taken on a shipment-by-shipment basis under the price trigger as follows:

Where
P_M is the c.i.f. import price of the shipment expressed in domestic currency,
P_T is the trigger price (average 1986-88 reference price)

D is the percentage fall in the import price below the trigger price, $(P_T - P_M) / P_T$.
AT is the additional duty imposed above bound tariff rate.

If	$D \leq 10\%$	then	$AT = 0$
	$10\% \leq D \leq 40\%$	then	$AT = 0.27(P_T / P_M) -0.3$
	$40\% \leq D \leq 60\%$	then	$AT = 0.39(P_T / P_M) -0.5$
	$60\% \leq D \leq 75\%$	then	$AT = 0.47(P_T / P_M) -0.7$
	$D \leq 75\%$	then	$AT = 0.52(P_T / P_M) -0.39$