

Institute for Agriculture and Trade Policy

By Sophia Murphy, Trade Director
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Why the Peace Clause Must End

What is the Peace Clause?

Article 13 of the World Trade Organization (WTO) Agreement on Agriculture, entitled "Due Restraint" but popularly known as the Peace Clause, prohibits countries from challenging other countries' use of export subsidies and domestic support programs that are otherwise permitted under the agreement's rules. More specifically, subsidies covered under Article 6.5 (the Blue Box) or the Aggregate Measure of Support (Amber Box) can face countervailing duties, but Members must exercise "due restraint" in imposing the duties. The Peace Clause specified that to be protected by the article, spending under the Blue and Amber Boxes could not exceed 1992 levels. Annex 2 (the Green Box) is even more fully protected by the Peace Clause, with no requirement to stay below 1992 spending levels. None of these subsidies can be challenged simply because they undermine trade privileges won under other agreements under the WTO, such as the Subsidies and Countervailing Measures Agreement (SCM). For example, the SCM allows Members to take action against subsidies that undermine their exports to a third country. Under the Peace Clause, agricultural subsidies cannot be challenged, even if they undermine a country's export performance. Export subsidies were also included under the Peace Clause, and are similarly protected from challenge, with the admonition to exercise due restraint.

The Peace Clause was to last nine years from when the Uruguay Round agreements came into effect, and is assumed by most WTO members to expire on 31 December 2003. The European Commission has attempted to argue that the expiry should be measured against the marketing year of the products concerned, which would extend the clause until June 2004, but this interpretation has been widely rejected by other WTO members.

The Peace Clause was part of the bargain struck by the European Commission and the United States to break the deadlock on agriculture during the Uruguay Round. The failure to make progress on agriculture threatened to derail the many other negotiations in progress. The Peace Clause was of course unpopular with other negotiators, but they saw little choice if they wanted to get an agreement, and so they accepted it as a necessary compromise.

How has the Peace Clause worked?

The language of the clause is vague enough that, at least from a legal perspective, the restriction does not seem particularly strong. Exercising "due restraint" is at best a subjective matter, especially given the decidedly unrestrained amount of domestic and export support in question. Nonetheless, the Peace Clause has clearly discouraged countries from seeking redress under the Subsidies and Countervailing Measures Agreement, or under non-violation nullification or impairment provisions. Non-violation nullification or impairment describes actions that do not violate existing rules, but have the effect of either negating, or undermining, trade concessions. For example, a country might agree to lower its tariff on apples, but then create a new

barrier—say a quota on apple imports—that effectively puts up a barrier as significant as the tariff was. In the case of agriculture, if domestic support payments are used to subsidize exports, then commitments to reduce export subsidies are rendered ineffectual. In practice, the Peace Clause has ensured that countries able to use subsidies under the Agreement on Agriculture (by and large, but not exclusively, developed countries) have not found themselves subject to disputes, even if their subsidies violated other WTO agreements.

The Peace Clause has also contributed to dumping of agricultural products at prices below the cost of production. It has had a “chilling effect” on countries that might otherwise have sought to protect themselves from subsidized agricultural exports. Since the disciplines on domestic and export support were so weak as to effectively allow spending by developed countries to continue virtually unchanged, the Peace Clause locked in already prevalent dumping practices and closed off the possible recourse offered by existing GATT rules and other Uruguay Round agreements. Inclusion of agriculture within the WTO system came at a very heavy price.

Why is the Peace Clause controversial?

The essential problem with the Peace Clause is that it favors the most privileged countries at the expense of poorer member states. It legitimizes the use of trade distorting measures in an agreement ostensibly dedicated to their elimination. It inhibits countries from protecting themselves from behavior that flouts the basic principles of free and fair trade.

The existence of the Peace Clause also makes developing countries less willing to open their markets—a good or a bad thing, depending on your perspective. Still, it is hard to justify such a clear symbol of developed country hypocrisy; the rich countries seek access to developing country markets, and constantly lecture developing countries on the virtues of unilateral liberalization, yet refuse to curb their own trade distorting practices.

What is the likely fate of the Peace Clause?

Both the European Union and the United States want the Peace Clause extended, and they are the most powerful actors in the WTO. However, an extension does not look likely at this late date. The general expectation is that the General Council meeting on December 15 will be like other such meetings at the WTO since Cancun – an airing of known positions with no real attempt to bridge differences. It is very difficult to see how negotiations can take place in this context. Without a negotiation, it is unlikely that even WTO members as powerful as the EU and the United States can extend a privilege that benefits them (and a handful of other OECD members) at the expense of the vast majority of countries.

The most vocal advocate for maintenance of the Peace Clause is the European Commission. The Commission is of course concerned to protect its Common Agricultural Policy (CAP) from attack. The CAP relies on tariffs, domestic support and export subsidies, each of which is disciplined under the WTO rules. The Peace Clause ensures that only the very minimal changes required under the Agreement on Agriculture would bind countries' spending, rather than the more fundamental rules of the GATT, and the WTO Agreement on Subsidies and Countervailing Measures.

The United States is also a strong advocate of the Peace Clause, although it is careful not to draw attention to its position, as support for the Peace Clause runs counter to its self-declared “ambitious” agenda for increased liberalization of agricultural trade. The U.S., in its switch from payments to agricultural producers linked to limiting production to so-called decoupled payments that are really a form of direct income support, has seen expenditures on agriculture soar since the WTO Agreement on Agriculture came into effect. The domestic support levels make it vulnerable to disputes—Brazil has already launched a dispute against US cotton subsidies.

The Peace Clause was remarkably absent from the draft negotiating texts that circulated earlier in 2003, reflecting the difficulty countries had with calling publicly for its extension. Most WTO Members want its expiry, and saw no reason to mention it, since the expiry was already written into the existing rules. It seemed the Peace Clause advocates assumed they could negotiate for its inclusion once negotiations on the rest of the text were underway. The failure of developed countries to persuade developing countries they are serious about agricultural liberalization in Cancun has severely damaged the prospects of agreeing to new rules for agricultural trade any time soon. Had negotiations been in full swing, there would have been several plausible scenarios for how the Peace Clause might have been extended, perhaps even without much being sought in exchange. Developing countries are heavily dependent on agricultural exports and might have judged it necessary to give the Peace Clause again, perhaps only for a year or two, to keep the big players at the table. In the context of the current stalemate, however, developing countries have no reason to renew an anyway offensive measure that privileges the rich at the expense of the poor.

What happens without the Peace Clause?

There is some expectation that countries will respond to the lapse of the Peace Clause with a flurry of cases against both EU and US subsidy use. The legal arguments are not cut and dry—the Agreement on Agriculture is actually at odds with the Agreement on Subsidies and Countervailing Measures, so a determination would be needed as to which applied in a given case. The European Commission has also said that disputes brought against agricultural subsidies would have to demonstrate harm *since* the expiry of the Peace Clause, which would mean several years of further inaction, while the necessary damage was inflicted. Despite such rather desperate arguments, which would probably not stand up in a legal case, it is clear that both importing countries and competing exporters would have solid grounds for complaint if they chose to mount a dispute.

There is good reason to suppose that the already very busy Dispute Settlement Body will not suffer unduly, at least at first. It is very difficult to show harm to a sector like agriculture. In manufacturing, production tends to be concentrated in a relatively small number of firms, which are often already linked in trade associations. Agricultural production, however, especially in developing countries, is the work of thousands, sometimes millions, of individual peasant farmers. They may associate in a union of some kind, but they are unlikely to have the means to demonstrate harm to a large percentage of their number as a result of subsidized imports to their domestic market. Cases are also expensive and complicated to mount, even when the evidence is overwhelming.

There is also the essential problem of power—for most would-be plaintiffs, the U.S. and E.U. are major trading partners, much more important to the developing country

as a trading partner than the developing country is to the U.S. or E.U. It takes considerable courage to risk this relationship for a case that may or may not be won. Until the rules to show harm are changed to simplify the process and make it more accessible to poorer countries, challenges to agricultural subsidies and dumping practices are likely to remain relatively few.

This does not make the extension of the Peace Clause a matter of indifference—far from it, and not only because the Peace Clause is a symbol of power trumping justice. Without the Peace Clause, Members will at last be permitted to exercise their fundamental rights in relation to agriculture, which is one of the primary engines of development. With political progress on new rules at a stalemate, it is time to see what the legal machinery of the WTO can do to enforce a fairer multilateral trading system for all. The expiration of the Peace Clause comes at a time when negotiations are stuck and may usher in a period of increased emphasis on policy through interpretation of the WTO's existing rules rather than through the agreement of new political bargains. Moreover, the threat of cases against existing subsidy practices may in itself drive recalcitrant WTO Members back to the negotiating table.

Whatever the impact over the next few months, it is clear that the Peace Clause's time has come. May it die quietly on December 31, 2003¹.

Article 13

Due Restraint

During the implementation period, notwithstanding the provisions of GATT 1994 and the Agreement on Subsidies and Countervailing Measures (referred to in this Article as the "Subsidies Agreement"):

- (a) Domestic support measures that conform fully to the provisions of Annex 2 to this Agreement shall be:
 - (i) non-actionable subsidies for purposes of countervailing duties¹;
 - (ii) exempt from actions based on Article XVI of GATT 1994 and Part III of the Subsidies Agreement; and
 - (iii) exempt from actions based on non-violation nullification or impairment of the benefits of tariff concessions accruing to another Member under Article II of GATT 1994, in the sense of paragraph 1(b) of Article XXIII of GATT 1994;

- (b) Domestic support measures that conform fully to the provisions of Article 6 of this Agreement including direct payments that conform to the requirements of paragraph 5 thereof, as reflected in each Member's Schedule, as well as domestic support within *de minimis* levels and in conformity with paragraph 2 of Article 6, shall be:
 - (i) exempt from the imposition of countervailing duties unless a determination of injury or threat thereof is made in accordance with Article VI of GATT 1994 and Part V of the Subsidies Agreement, and due restraint shall be shown in initiating any countervailing duty investigations;
 - (ii) exempt from actions based on paragraph 1 of Article XVI of GATT 1994 or Articles 5 and 6 of the Subsidies Agreement, provided that such measures do not grant support to a specific commodity in excess of that decided during the 1992 marketing year; and
 - (iii) exempt from actions based on non-violation nullification or impairment of the benefits of tariff concessions accruing to another Member under Article II of GATT 1994, in the sense of paragraph 1(b) of Article XXIII of GATT 1994, provided that such measures do not grant support to a specific commodity in excess of that decided during the 1992 marketing year;

- (c) Export subsidies that conform fully to the provisions of Part V of this Agreement, as reflected in each Member's Schedule, shall be:
 - (i) subject to countervailing duties only upon a determination of injury or threat thereof based on volume, effect on prices, or consequent impact in accordance with Article VI of GATT 1994 and Part V of the Subsidies Agreement, and due restraint shall be shown in initiating any countervailing duty investigations; and
 - (ii) exempt from actions based on Article XVI of GATT 1994 or Articles 3, 5 and 6 of the Subsidies Agreement.

¹ "Countervailing duties" where referred to in this Article are those covered by Article VI of GATT 1994 and Part V of the Agreement on Subsidies and Countervailing Measures.