

18 January 2012

# Screening report

## Iceland

### Chapter 30 – External relations

**Date of screening meetings:**

Explanatory meeting: 10 April 2011

Bilateral meeting: 19 May 2011

## **I. CHAPTER CONTENT**

The *acquis* in this field consists mainly of directly applicable EU legislation which does not require transposition into national law. This EU legislation results essentially from the EU's multilateral and bilateral commitments in the trade field, as well as from a number of autonomous trade measures.

In this context, applicant countries are required to progressively align their policies towards third countries and their positions within international organisations (most notably WTO) with the policies and positions adopted by the European Union and its Member States, so as to be able to implement the EU common commercial policy upon the date of accession.

In the area of humanitarian and development policy, Member States need to comply with EU legislation and international commitments and ensure the capacity to participate in the EU's development and humanitarian policies.

Legislation under this chapter is not covered by the EEA.

## **II. COUNTRY ALIGNMENT AND IMPLEMENTATION CAPACITY**

Iceland indicates that it can generally accept the *acquis* regarding external relations and that it does not expect any difficulties to implement the *acquis* by the time of accession.

Iceland declares that it will provide adequate capacity to secure its participation in the EU's common commercial policy as well as in the EU's development and humanitarian policies.

However, Iceland indicates that application of some parts of the *acquis*, notably regarding the EU external tariff, might affect its fisheries and aluminium industry. Iceland indicates that denouncing of its free trade agreement would have an effect on its market access in third countries, in particular its historical trade relations with the Faroe Islands. Iceland identified difference in its WTO positions to those of the EU with regard to agriculture and fisheries.

### **II.a. Common commercial policy**

The trade policy of Iceland is determined by its membership in the WTO, the EFTA agreement and the European Economic Area.

Iceland ratified the General Agreement on Trade and Tariff (GATT) in 1968 and is a founding member of the World Trade Organisation. Iceland is a party of the Government Procurement Agreement (GPA) since 2001. The majority of Iceland's trade legislation mirrors WTO and EEA obligations and is encoded in a number of acts, with the Customs Act from 2005 regulating most of its trade.

Within the WTO, Iceland negotiated high bound rates, but it applies lower rates, on average. The simple average Icelandic most favoured nation (MFN) bound ad valorem tariff rate for agricultural products is 43.2%, for fish and fishery products 2.8% and for other goods 9.8% with an overall simple average of 13.4%. The simple average Icelandic MFN applied tariff rate for agricultural products is 6.4%, for fish and fishery products 1.3% and for other goods 2.4%. Iceland states that application of the higher EU tariff for imports of fishery products (11.8%), especially with respect to fish for processing, might negatively impact the competitiveness of its

fisheries. The EU tariff on certain raw material could potentially have the same effect (e.g. bauxite).

Iceland has undertaken commitments in the General Agreement on Trade in Services (GATS) in 9 out of 12 service sectors (business services, telecommunications, construction and engineering, distribution, financial, tourism, environmental, cultural and sporting, and transport).

Trade defence instruments are defined in the Customs Act, although Iceland has never used trade defence instruments, so far. Iceland has not been involved in the WTO dispute settlement mechanism. It has participated as a third party in 6 cases and exercises this right under the current DS400 and DS401 case (EU-Seal case).

Iceland is active in the Doha negotiation round. It is a member of the G-10 group of highly developed countries and is willing to undertake commitments in agriculture. However, the proposed reductions in tariffs that it advocates are lower than the proposals by the EU. Iceland is a member of the Friends of Fish and advocates for stronger discipline on fisheries. It favours an ambitious outcome on industrial products in particular regarding products for the fishing industry, fish and fish products. Its positions are sometimes not the same as the EU's, namely in agriculture and fisheries. In order to avoid that its policy be in opposition to the EU in the WTO, Iceland agreed to hold regular consultations with the EU on the above mentioned issues.

Iceland grants a Generalised System of Preferences (GSP) to 50 countries. The treatment and its exceptions are defined by Regulation 119/2002. The main beneficiary is Bangladesh with over 60% of total customs value. The value of GSP imports in 2010 amounted to €3.5 million. Iceland states that it will implement the EU GSP Regulation (EC) No 732/2008 upon accession to the EU.

Iceland has generally no duties on textiles. It applies 15% MFN duty on clothing products. Trade in textiles and clothing products is not subject to any other import duty or quantitative restriction. Iceland states that Regulations (EC) No 3030/93 and 517/94 on quantitative restrictions and surveillance measures applicable for textile products will take direct effect upon accession.

Export credits are provided by the Export Credit Guarantee Department of the New Business Venture Fund and regulated by Act on New Business Venture Fund 61/1997. The fund is an independent entity owned by the state. The export credits guarantees were established for the purpose of increasing Icelandic export to countries with extraordinary financial and/or political risk. The Export Credit Guarantee Department does not provide direct credits/financing, refinancing, interest-rate support or aid financing, but merely export credit insurance and guarantees. The guidelines of the Export Credit Guarantee Department on risk valuation and premium decisions are based on OECD and Berne Union recommendations. The export guarantee fund does not provide short-term export guarantees covering OECD countries. Regarding long- and medium-term loans, Iceland states that its methodology is already in line with the principles of Directive (98/29/EC) on harmonisation of the main provisions concerning export credit insurance for transactions with medium and long-term cover.

Iceland controls exports of dual use goods in a similar manner as prescribed by the EU regime. It applies the catch-all principle in executing these controls, however, the list of controlled items is not the same as prescribed by Regulation (EC) No 428/2009 setting up a regime for the control of exports, transfer, brokering and transit of dual-use items. Iceland is currently preparing a regulation that will implement rules identical to those in the EU regulation. In 2011, Iceland applied for participation in the Wassenaar Arrangement on export controls for conventional arms and dual-use goods and technologies. Iceland states that by the date of the accession, it will apply the dual use control system of the EU and will have the adequate administrative capacity.

Iceland is not a participant of the Kimberly process and does not apply any provisions of Regulation (EC) No 2368/2002 implementing the Kimberley Process certification scheme for international trade in rough diamonds. Similarly, Iceland does not apply any trade controls prescribed in Regulation (EC) No 1236/2005 concerning trade in certain goods which could be used for capital punishment, torture or other cruel, inhuman or degrading treatment or punishment. Iceland states that by the date of accession, it will apply both regulations.

## **II.b. Bilateral agreements with third countries**

Iceland is a member of the European Economic Area and EFTA. It has an additional 22 FTAs concluded within the EFTA framework with 31 countries.<sup>1</sup> As a rule, Iceland negotiates FTAs within the EFTA framework, but it negotiates individually the parts covering agricultural products.

Iceland has also concluded bilateral free trade agreements. These are, as follows: two with the EU, an FTA with the EU from 1972 (mostly superseded by the EEA) and a agreement on trade in basic agricultural products, based on Article 19 of the EEA; two agreements with Denmark on trade with Greenland and with the Faroe Islands. The latter is the only agreement by which Iceland establishes free trade for all agricultural products, a sector that usually remains protected in other FTAs.

Iceland is currently negotiating new FTAs (within the EFTA framework) with Algeria, Bosnia and Herzegovina, Hong Kong India, Indonesia Montenegro,, , Thailand, and the three members forming the Russia, Belarus and Kazakhstan customs union. It is also bilaterally negotiating an FTA with China.

Furthermore, EFTA is conducting dialogues in view of possible future free trade negotiations with Vietnam and Central American countries (Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua and Panama).

The EFTA framework also establishes trade relations through Joint Declaration on Cooperation with Malaysia, Mauritius, Mongolia, Central American States and Vietnam. This form of cooperation can lead to future FTAs.

Iceland holds consultations on trade with USA, Poland, Japan, China, Russia and Germany.

All FTAs, with the exception of the bilateral agreement on agriculture with the EU, include a withdrawal clause which needs to be invoked 6 or 12 months prior to the desired termination. The agreement with the Faroe Islands stipulates that its provisions for investors and service providers, shall remain in place for a period of at least five years after the termination of that agreement.

Iceland agrees to apply the trade agreements that the EU has concluded with third countries and denounce all its current free trade agreements by the date of accession. It states that denouncement of the agreements will have an effect on its market access in third countries, as well as importation of goods and services to Iceland. It states that the denouncement of the FTA with the Faroe Islands will have the most important economic impact.

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<sup>1</sup> Albania, Canada, Chile, Colombia, Croatia, Egypt, the Gulf Cooperation Council (GCC; comprising Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates), Israel, Jordan, the Republic of Korea, Lebanon, the Former Yugoslav Republic of Macedonia, Mexico, Morocco, Palestinian Authority, Peru, Serbia, Singapore, the Southern African Customs Union (SACU; comprising Botswana, Lesotho, Namibia, South Africa and Swaziland), Tunisia, Turkey and Ukraine.

Iceland has signed Bilateral Investment Agreements (BITs) with 12 countries. Two BITs were concluded within the EFTA framework and are parts of respective FTAs (South Korea, Singapore), two are with EU member states (Latvia, Lithuania) and another 8 are bilateral agreements (Chile, China, Egypt, India, Lebanon, Mexico, Uganda and Vietnam ). The provisions enabling investors to transfer funds have been recently modified in view of Iceland's capital restrictions under the IMF arrangement. Iceland stated that most of its BITs would need to be amended in order to be brought in line with the *acquis*.<sup>2</sup> Iceland indicated its preparedness to bring the above mentioned BITs in line with the *acquis*.

### **II.c. Development policy**

Iceland is a well established donor country. Its official development assistance (ODA) was steadily rising in the run up to the economic and financial crisis. From 0.12% of GNI in 2000, it reached 0.37% of GNI in 2008. It has since decreased to 0.22% of GNI. Iceland aims at raising this percentage gradually over the coming years with ODA reaching 0.28% in 2014, 0.5 in 2017 and 0.7 in 2019.

Iceland's International Development Co-operation is based on Act 121/2008. The Act is holistic and covers bilateral and multilateral development cooperation as well as humanitarian aid, emergency assistance and peace-building efforts. According to the act, a proposal for a parliamentary resolution concerning a strategy for Iceland's development co-operation for the period 2011-2014 was submitted to Parliament in February 2011 and adopted in June 2011.

Iceland's development policy priorities are set out in the Strategy of Iceland's Development Cooperation 2011-2014. It has three thematic areas of intervention; natural resources (energy, fisheries), human capital (education, health) and peace building (governance, reconciliation). Gender equality and protection of environment are horizontal priorities cutting across all three thematic areas. As Iceland is not a member of the OECD/DAC committee, the strategy foresees application for membership of the committee. The strategy also covers humanitarian interventions.

The majority of Iceland's ODA is channelled through multilateral cooperation, particularly through the UN. Within the UN system, the biggest recipient is the United Nations University (UNU). The UNU programme based in Iceland comprises three components: fisheries, geothermal energy and land restoration. Bilateral cooperation is implemented by the Icelandic International Development Agency (ICEIDA). The Strategy 2011-2014 identifies Malawi, Mozambique and Uganda as priority countries. Special attention is also given to peace-building in Afghanistan and support to Palestine refugees by means of contributions and secondments of experts to international organisations. Four multilateral agencies are identified as key institutions: The World Bank Group, UNICEF, UN Women and the United Nations University.

Iceland stated that it is committed to the Millennium Development Goals, the Monterrey Consensus on financing for development, the Paris declaration on aid effectiveness and the Accra agenda for action.

### **II.d. Humanitarian aid**

Humanitarian and emergency assistance made up 11% of Iceland's ODA in 2010. It is delivered via financial contributions to multilateral organisations, assignment of experts to these organisations and through the emergency response of Icelandic NGOs and the Icelandic Search and Rescue Team. Over half of Icelandic humanitarian assistance goes through UN agencies,

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<sup>2</sup> ECJ rulings C-249/06, C-205/06, C-118/07.

and a further third through NGOs. In 2010, around 15% went to emergency assistance in Haiti through the Search and Rescue Team, Landbjörg, which has expertise in earthquake rescue. Landbjörg participates in the national Coordination Centre of the Civil Protection. The centre is connected to the EU's Monitoring and Information Centre (MIC) in Brussels.

The Act on Development Cooperation which covers also humanitarian aid does not explicitly spell out the principle of non-discrimination as the guiding principle of humanitarian interventions, as prescribed in Regulation (EC) 1257/96 concerning humanitarian aid. However, Iceland states that it applies the non-discrimination principle in its humanitarian interventions. In this context, guidelines for co-operation with NGOs that provide humanitarian and emergency assistance were revised and updated in 2010. The new guidelines also cover co-operation with NGOs engaging in development co-operation. They include all measures set forth in the Regulation (EC) No 1257/96 concerning humanitarian aid, including the principle of non-discrimination.

### **III. ASSESSMENT OF THE DEGREE OF ALIGNMENT AND IMPLEMENTING CAPACITY**

Overall, Iceland has already reached a high level of alignment with the *acquis* in the field of external relations. The EU is its main trading partner and changes in commercial relations with third countries, which will follow the application of the common commercial policy, shall have no major effect on Iceland's economy. Iceland has a long tradition of multilateral commercial cooperation, as a member of the EFTA and WTO, and has therefore developed good administrative capacity in this area. Regarding development policy and humanitarian aid, Iceland has a well developed system for assisting development countries and deploying humanitarian interventions. Iceland is well prepared to successfully participate in EU development and humanitarian policies.

Iceland has identified remaining gaps in view of full application of the *acquis* in the field of external relations and has committed itself to introducing necessary changes in its legislation in order to meet EU obligations upon its accession. Most notably, it will denounce the existing bilateral free trade agreements (FTAs) or introduce necessary amendments in the bilateral investment treaties (BITs).

Iceland raised its concerns about the EU external tariff for fish and fishery products due to the higher EU rate. Iceland does not commit to align itself to EU positions in the WTO, particularly with regard to agriculture and fisheries. Final decisions however will be made when defining a negotiating position on this chapter.

#### **III.a. Common commercial policy**

Iceland needs to apply the EU common commercial policy at the time of accession. The level of alignment is already very high in view of the country's membership of the EEA and the OECD. Gaps remain mainly in the area of export controls. Alignment has already started with regards to control of dual-use items. In this area, the draft Icelandic regulation plans to imitate the EU regulation, but it will go beyond the EU regime by prescribing export controls of services involving dual-use goods. Upon accession, the regulation establishing a regime for control of the dual-use items, the regulation arising from the Kimberly process obligations and the regulation governing trade with materials which could be used for torture will take direct effect and will need to be implemented by the export control administration.

Changes in external tariffs and the application of the EU GSP regime will not affect the Icelandic economy. Iceland claims that changes of the fish related tariffs for which there is a significant

gap between the current Icelandic tariff and the EU tariff might affect its economy. The simple average Icelandic most favoured nation (MFN) bound ad valorem tariff rate for fish and fishery products is 2.8%. The average Icelandic MFN applied tariff rate for fish and fishery products is 1.3%. The simple average EU MFN bound ad valorem tariff rate for fish and fishery products is 12.7%. The average EU MFN applied tariff rate for fish and fishery products is 11.2%. Despite the large gap, the impact will probably be limited. Iceland imports only small amount of fish and fisheries products (e.g. about €50 million in 2009). Moreover, in case of imports of raw fish under the customs procedure "inward processing", the processing is allowed without the payment of import duty under the condition that the processed products are re-exported to third countries.

Iceland's commitments under GATS are similar to those of the EU. Differences can be retained, as long as they do not prevent countries from applying the *acquis*. Iceland's schedule of GATS commitments in the financial sector currently does not include a market access limitation regarding undertakings for collective investment in transferable securities (UCITS). For EU Member States, the UCITS limitation derives from an EU Directive, which Iceland will need to implement by accession and will therefore need to modify its GATS commitments. In the area of transport services, Iceland has undertaken more liberal commitments than those prevailing in EU Member States, however, they do not need to be modified yet.

Iceland has so far taken some positions, particularly in the Doha round, which are different from those of the EU. Iceland's proposals for future tariffs in agriculture are higher than those proposed by the EU. Iceland has also participated as a third party in the WTO dispute settlement on seals taking a position contrary to EU's legal claims. Iceland has not committed to align to the EU position and where divergences occur, including in the DDA negotiations and in dispute settlement cases, it needs to commit to enter into discussions with the Commission in order to progressively align its position to that of the EU. Iceland will need to align its positions in the WTO with those of the EU upon accession.

### **III.b. Bilateral agreements with third countries**

Iceland needs to denounce all its free trade agreements (FTAs) before accession to the EU. All Iceland's FTAs include provisions which enable the country to withdraw from those agreements. The impact will be greatest in the case of the Iceland-Faroe Islands FTA, however, to a lesser extent for Iceland than for the Faroe Islands. The Faroe Islands' exports to Iceland are 4% of its total exports.

Iceland has a small number of Bilateral Investment Treaties (BITs). These BITs (including those with two EU Member States) include clauses which are not compatible with the *acquis*. The BITs with the two EU Member States need to be phased out or terminated as of accession. Others will have to be brought in conformity with the *acquis* by the date of accession.

### **III.c. Development policy**

The objectives, methods and instruments of Iceland's development policy are in line with those of the EU. Iceland's official development assistance is comparable to the EU average, but has been recently significantly affected by the economic crisis. The plans to return to high previous levels are credible and already in the process of implementation. In development interventions, Iceland has well deployed its expertise in exploitation of thermal waters, sustainable fishing and gender equality policies. Iceland is encouraged to take verifiable national actions to reach the planned 0.7% ODA/GNI by 2021.

### **III.d. Humanitarian aid**

Iceland is already part of the EU humanitarian interventions coordinated through the Monitoring and Information Centre (MIC). The percentage of its external assistance devoted to humanitarian aid reflects that of the EU. Application of the non-discrimination principle as inscribed in the Regulation 1257/96 is well respected although it is not prescribed in the law.