

10 June 2011

Screening report

Iceland

Chapter 11 – Agriculture and Rural Development

Date of screening meetings:

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Bilateral meeting: 24 - 27 January 2011

I. CHAPTER CONTENT

The *acquis* on agriculture and rural development covers a large number of binding rules, many of which are directly applicable. The proper application of these rules and their effective enforcement by an efficient public administration are essential for the functioning of the Common Agricultural Policy. This requires the setting up of a paying agency and management and control systems such as the Integrated Administration and Control System and the capacity to implement rural development actions. Member States must be able to apply EU legislation on direct support schemes and to implement the common market organisation for various agricultural products.

The *acquis* under this chapter is not covered in the EEA Agreement, except for organic farming. Article 19 of the EEA Agreement provides for progressive liberalisation of trade in agricultural products between Iceland and the EU. Additional bilateral trade preferences, negotiated under Article 19 of the EEA Agreement, entered into force on 1 March 2007.

The implementation, management and control of the Common Agricultural Policy (CAP) require the creation, modification and/or reinforcement of appropriate administrative structures. In some cases the *acquis* sets out, to a greater or lesser extent, detailed specifications for the required administrative structures.

The required administrative structures are not always specified in the *acquis*. In many cases the *acquis* simply uses terms such as the “competent authority” to refer to the administrative structure that is needed. This means that it is left to each Member State to decide which institution is responsible for effective implementation of the *acquis*. However, the functions that EU Member States must have the capacity to carry out - through the administrative structures they establish - are clearly specified in the *acquis*.

II. COUNTRY ALIGNMENT AND IMPLEMENTATION CAPACITY

This part summarises information provided by Iceland and the discussion at the screening meeting. Amounts are mostly indicated in Icelandic krónur. The present (March 2011) exchange rate is 1€ = 160 ISK but it should be noted that the króna has over the years depreciated substantially in relation to the euro.

Iceland acknowledged that the *acquis* on agriculture and rural development forms the basis for the negotiations. They underlined that Iceland's agriculture is in a particular situation that cannot be compared with any other European country due to its severe climatic conditions. Iceland asked to take these conditions into account in the accession negotiations, in particular with a view to the disadvantages of Icelandic farmers caused by the climate and the need of the small Icelandic administration to avoid complicated administrative procedures. Iceland will include proposals in this regard in its negotiation position.

Iceland indicated that its agricultural policy and administration is tailor-made to the domestic circumstances, scope and nature of agriculture. Iceland has therefore indicated that it does not intend to make changes in policy, administration or its legislation until the Accession Treaty has been accepted in a referendum in Iceland. Iceland has however stated that all necessary preparations will be undertaken so that, after the referendum, changes of policy, administration and legislation can be implemented in a timely way in order to respect obligations upon accession.

Agriculture in Iceland is characterised by difficult climatic conditions with a short and cold growing season, extreme weather and low yields. The volcanic soils are prone to erosion and the number of plant species is limited. Rural areas are sparsely populated and production and transport costs are high.

The range of agricultural products is limited and covers approximately 50% of total domestic food needs. There are around 3400 farms in Iceland, predominantly occupied in livestock production, accounting for approximately 87% of gross farm income. In-wintering of all livestock is necessary. Production of arable crops is very limited while there is some production of potatoes and vegetables, including production in green houses.

Agricultural policy in Iceland is based on two main legal acts:

- Act No 99/1993 on the Production, Pricing and Sale of Agricultural Products, which lays down the policy framework as well as provisions for production control, provisions on slaughter and processing, market measures and producer support.
- Act No 70/1998 on Agriculture, which lays down provisions for development projects, extension services and livestock improvement

Iceland's agricultural policy focuses on food security, food safety and food quality, maintaining and strengthening rural activity, environmental sustainability and maintaining farm income. The main objectives of Iceland's agricultural policy, as stated in Act No 99/1993 are:

- Promotion of structural adjustments and increase of efficiency
- Guarantee sufficient supply of domestic agricultural products
- Income of farmers to be equitable with that of comparable occupations
- Use of domestic inputs in order to promote security of production and employment
- Equality between producers with respect to output prices and access to markets.

Overall responsible for agricultural policy is the Ministry of Fisheries and Agriculture that covers policy making, overall control issues as well as certain direct administrative tasks. The Food and Veterinary Authority (MAST) is responsible for a range of administrative tasks that involve direct contact with the producers. Iceland stated that its administration is small and cost-efficient with a small number of staff and relatively simple procedures. The Farmers Association, including its local branches and local authorities, are involved in the implementation of agricultural support, including payment to the farmers.

Icelandic agriculture receives a high level of support. The Produced Subsidy Equivalent (PSE), as calculated by the OECD, is 47% of the total value of agricultural receipts in 2009. (EU-PSE was 23% in 2009). In addition to import tariffs on agricultural products entering Iceland, farmers receive financial support through direct payments. Direct payments are granted to livestock producers, dairy producers and producers of certain greenhouse products (tomatoes, cucumbers and sweet peppers). Price controls apply only to the dairy sector with both minimum producer prices for farm gate milk and for certain dairy products. Supply control is also applied only in the milk sector via a quota system.

II.a Horizontal

The direct support schemes are based on the Act on the Production, Pricing and Sale of Agricultural Products No 9/1993 and on binding and renewable agreements between the Government and the Farmers Association. The three agreements are:

- The Agreement on dairy production from 2004, expires 2014
- The Agreement on sheep production from 2007, expires 2015

- The Agreement on horticultural production from 2002, expires 2013.

The agreements are binding for the Government and financed annually through the state budget.

MAST plays an important role with regard to the management and control of the direct support schemes. It keeps a number of registers on which all payments for support schemes are based. The most important registers are; Register of payers of agricultural production levy, Register of right holders of support entitlements for milk production, Register of right holders of support entitlements for sheep production, Register for receivers of direct payments in horticulture, Register of agriculture holdings with payment entitlements, Registers for headage payment and quality payments for sheep production. The Farmers Association keeps and maintains a number of the registries, by law or an agreement with MAST or the Ministry for Fisheries and Agriculture.

In addition, the administration of the support schemes is based on a number of computerised databases such as MARK that is used for individual identification of livestock, BÚSTOFN that collects information from livestock officers as well as AFURÐ that is used for slaughterhouses and processing plants. These databases are operated by the Farmers Association. Livestock officers are employed by municipalities and check animal welfare, food supply and collect numbers of animals.

Financial control of agricultural expenditure is based on the following legal framework:

- The Act on the Production, Pricing and Sale of Agricultural Products No 99/1993
- Regulation No 4/2011 concerning direct payments in horticulture
- Regulation No 913/2010 concerning entitlements in milk in registered farms and payments to farmers for the production year 2011
- Regulation No. 11/2008 on entitlements for sheep on registered farms
- Regulation No. 10/2008 on stipulating conditions and management according to quality control scheme for sheep farming.

The Farmers Association manages the individual payments to holders of entitlements provided that all relevant conditions are fulfilled. The Farmers Association receives payments from the Ministry of Finance on the basis of a cash flow plan for each month of the year that needs to be confirmed in advance by the Ministry of Fisheries and Agriculture. The Ministry of Fisheries and Agriculture reviews the overall accounts on a monthly basis. The Icelandic National Audit Office audits all Ministry books and receives all accounts from the Farmers Association.

The municipalities are responsible for surveillance of livestock. The Soil Conservation Service of Iceland has control functions as regards the general conditions of the grazing areas.

The surveillance of the support scheme in the livestock sector is regulated by Act No. 103/2002 on Livestock Management and Regulation No. 743/2002 on Livestock Surveillance.

- The surveillance is the direct responsibility of the municipalities who employ livestock officers. MAST coordinates their work and collects data into a database. The Farmers Association is responsible for coordinating the task.
- Every autumn a form is sent to all livestock owners who are obliged to return it before 20 November with indications of the number of animals, the quantity of feed, livestock houses and grazing areas. From 2010 it has been possible to do this registration on-line.
- Before 15 April livestock officers undertake an on-the-spot check of every farm or establishment that has registered livestock.

The agricultural policy of Iceland is financed primarily from the annual state budget in accordance with the agreements with the Farmers Association (as mentioned above). The budget amounts to ISK 11015 million (€ 68.8 million) in 2011. In addition the agricultural production levy is used which amounted to 366 million ISK (€ 2.3 million) in 2008 and is based on 1.2% of the agricultural turnover. The levy is divided between the Farmers Association, including its local and sectoral branches and the Emergency Relief Funds (37 million ISK). Finally a number of so-called pre-allocated levies (420 million ISK) are applied for dairy products and for marketing of sheep and horse products (see further below).

State aid for agriculture in Iceland consists mainly of direct payments to farmers. In addition there are several smaller payments which comprise, amongst others, measures to support marketing of certain products, support for extension services, livestock improvement, electricity subsidies for greenhouses, utilisation, storage and marketing of wool as well as education and research. In terms of rural development, there are several budget headings supporting an array of projects like organic farming, grain cultivation, grazing control and land utilisation, environmental efforts, drainage and calcium spreading on fields and diversification. The state further supports five regional programmes for afforestation and several soil conservation programmes.

Trade measures are based on the WTO agreement, the EEA, more than 20 Free Trade Agreements negotiated jointly with the EFTA-states (separate bilateral agreements on agriculture) and agreements with Norway and the Faroe Islands. Export subsidies were abolished in 1992.

Iceland applies relatively high import customs duties on most agricultural products that are produced in Iceland. The duties vary according to the agreement they are based on. Iceland states that their Most Favoured Nation (MFN) tariff is 30% ad valorem and a specific rate of duty varies from 5 ISK/kg to 1462 ISK/kg. For the WTO minimum access quotas, e.g. meat, dairy products and processed meat, the in-quota tariff rate is 32% of the base rate of duties in the Icelandic WTO schedule. For the WTO current access quotas e.g. flowers and other plants, products and vegetables, Iceland stated that the in-quota tariff rate is up to 30% ad valorem. Many current access commitments under WTO are not subject to any quota system upon import due to the fact that applied MFN rates are lower than in quota rates.

The collection and production of **farm account statistics** is based on Act No. 63/1989 on the Agricultural Economics Institute that lays down provisions for collection of economic information on farms and their use. Act No. 99/1993 outlines the requirements for agricultural accounts. Farmers are not obliged to keep official farm accounts and information is not available on the share and type of farms currently keeping accounts on a voluntary basis. Accountancy information was collected from over 300 farms for the accounting year 2009 of which the majority were dairy farms and sheep farms.

As regards **Non-Annex I products**, the Act on Production, Pricing and Sale of Agricultural Products provides for:

- a levy on imports of processed agricultural products containing raw material that is also produced in Iceland. This levy shall not be higher than the price difference between the price of the raw material on the domestic market and the world market. The levy, although never utilised, is reimbursable upon re-export of the processed goods.
- a price compensation mechanism available for exported processed agricultural products that fulfil a number of conditions. The mechanism is however only used to a limited degree (2.7 million ISK budgeted in 2011).

II.a. Common market organisation

II.a.1 Arable crops, fibre, sugar

Production of arable crops in Iceland is very limited. Climate only allows cultivation of one cereal: barley. The surface of this crop has increased substantially from 200 ha in 1991 to 4000 ha in 2010, due to warmer climate and breeding of better adapted varieties. The average yield is estimated at 3.5 tonnes per hectare. Barley is almost exclusively used as fodder for the animals on the farm where it is grown. There is no market in domestic barley. Barley production is eligible for a subsidy of around 15000 ISK (€94) per hectare for the first 20 hectares and ca. 10000 ISK (€63) for the next 20 hectares. This support also applies for other fodder crops (excluding grass).

Iceland has no fibre crops or sugar production and hence no related specific measures. There is no commercial production of oil seeds in Iceland but a project experimenting with cultivation of oil rape is under preparation. In 2010 rape seeds were cultivated on 40-50 ha. There are no specific measures in this respect.

II.a.2 Livestock products

Most farm animals in Iceland belong to native breeds. Import of live animals is not allowed, although some new breeds have been introduced by import of semen and embryos, notably of beef breeds. Iceland indicated that, due to their long isolation, the native breeds are extremely vulnerable to imported animal diseases and that Iceland intends to raise this issue in the accession negotiations. The issue will be dealt with in chapter 12, Food safety, veterinary and phytosanitary issues.

Milk and milk products

The dairy sector, including beef, is the most important agricultural sector in Iceland with 47% of the agricultural turnover. Milk production amounted to 129 million litres in 2009 (0.1% of EU production). Almost all dairy farms are family farms and in most cases the farm is the main source of income for the family. Iceland's self-sufficiency rate is more than 100% for dairy products. The consumption of milk per capita is one of the highest in the world. Production of milk from sheep or goats for human consumption is minimal.

Iceland stated that milk production in Iceland is subject to a number of disadvantages such as the low yield per cow (5400 litres) and problems related to collection of the milk. Structural changes have been significant in the milk sector; from 1970 to 2008 the number of dairy farms fell from 3568 to 729.

The support to dairy farmers is regulated by the Act on the Production, Pricing and Sale of Agricultural Products No. 99/1993. The Act lays down that a binding agreement on dairy production must be made with the Farmers Association. Dairy farmers are supported mainly by direct payments, by a system of minimum producer prices (farm gate price) and by a milk quota regime. Support is also granted for breeding and development work.

Direct payments are provided as support entitlements based on the individual quota (4915 million ISK agreed for 2011) or headage payments based on the number of cows (581 million ISK agreed for 2011).

The producer receives the full headage payment for the first 40 cows but payments are gradually reduced for numbers of cows higher than 40. For numbers of cows above 100 no payment is made.

The Agricultural Pricing Committee sets a minimum producer price (farm gate price) for first-rate milk delivered within the production quota as well as the wholesale price for a number of dairy products, e.g. fresh milk, cream, butter, skyr, certain types of cheese, whole milk powder and skimmed milk powder. The minimum farm gate price applies in the whole of Iceland irrespective of the distance from the dairy. On 1 February 2011 the price was 74 ISK/ltr.

Dairies are partially exempted from competition rules. They can agree to make price transferrals between different products and/or make arrangements regarding division of labour for production of specific dairy products and/or cooperate in other ways to keep down costs of production, storage and distribution. The largest dairy cooperative has a share of 88% of milk received from farmers.

The above mentioned exemptions are facilitated by pre-allocated levies applied to dairy products:

- The price transferral levy (312 million ISK, est. 2011) is collected at delivery of milk to the dairy and used to lower the price of certain dairy products.
- The price equalisation levy (93 million ISK, est. 2011) is collected at delivery of milk to the dairy and used to level production costs between the dairies.

The production quota for milk is decided by the Minister of Fisheries and Agriculture for each year based on a recommendation from the Executive Committee for the implementation of national agricultural agreements. The aim is to ensure an appropriate supply of milk and milk products on the domestic market. There is no system of separate quotas for direct sales as direct sales are negligible. Milk production quotas can be transferred. Excess production must be exported without any public support or price equalisation. There is no limitation for such export.

Beef

The number of cattle in Iceland is approximately 73500 on 971 farms (2009). Cattle are sold directly from the farmer to the slaughterhouse and prices are determined by the market. Slaughtering is evenly spread over the year.

Due to the importance of dairy production in Iceland, production of beef and veal meat in Iceland is mostly a side product from the milk production. In recent decades the use of beef breeds has however developed (galloway, limousine, Aberdeen angus). Suckler cows which belong to the above mentioned breeds are eligible for twice the headage payment of dairy cows and are not subject to reduction on the grounds of herd size.

Identification of bovine animals is based on ear tagging and on the farm registers and databases for domestic animals. Transport of livestock without identification and the prescribed registration is prohibited. Iceland stated that the system is not in compliance with EU requirements, one difference being that only one ear tag is required. The issue will be dealt with in chapter 12 Food safety, veterinary and phytosanitary issues.

Sheep and goats meat

Sheep farming is spread all over Iceland and plays an important role in Icelandic agriculture. The number of farms possessing sheep is 2826 (2010). The total size of the flock is approximately

469000 winterfed sheep of which approximately 366000 are breeding ewes (2009). The main emphasis is on meat production with approximately 8800 tonnes annually. Iceland increased its export of sheep meat in recent years from around 1200 tonnes (2006) to 2400 tonnes (2009). Wool, skin and milk make up only 10% or less of net returns. Mountain grazing is practiced during the summer while in-house keeping is necessary during the winter. 97% of slaughtering takes place in September-October. Prices are determined by the market.

Sheep production is supported by direct payments. Support entitlements are originally based on historical production. They are transferable between farms and farmers. The total amount of support entitlements is 2228 million ISK (agreed for 2011). An additional 1165 million ISK (agreed for 2011) are paid out via the quality payments scheme on condition of compliance with requirements in the area of animal health, environment and animal welfare. Wool production is supported by 390 million ISK (agreed for 2011) for wool utilisation and 364 million ISK (agreed for 2011) for marketing and storage costs of sheep meat.

A levy for marketing of sheep meat (13 million ISK, 2010) is collected at wholesale level and used by the Sheep Meat Marketing Board.

Goat livestock in Iceland is very limited. Approximately 500 animals of traditional Icelandic breed (exclusively found in Iceland) are being kept for their preservation purpose. Products are for home consumption or direct sale.

Identification of sheep and goats is based on ear tagging and on the farm registers and databases for domestic animals. Transport of livestock without identification and the prescribed registration is prohibited. Iceland stated that the system is not in compliance with EU requirements, one difference being that only one ear tag is required, another being different types of ear cuts. The issue will be dealt with in chapter 12 Food safety, veterinary and phytosanitary issues.

Pig meat

There are 18 pig producers in Iceland that have a total of approximately 43000 pigs (2009). The number of slaughtered heads per year is 83867 (2009) producing 6375 tonnes of meat, reaching 97.2% self-sufficiency. There are 6 slaughterhouses for pigs in Iceland. Prices are determined by the market. Apart from import protection through tariffs there are no particular support measures in the pig sector.

Horse and Horsemeat

There are approximately 77000 horses in Iceland, all of the old native breed. A significant number of riding and breeding horses is exported every year which accounted for a value of 1064 million ISK in 2008. Iceland produced around 1000 tonnes of horsemeat in 2008. A levy for marketing of horse meat (2 million ISK, 2010) is collected at wholesale level and used for marketing by the Producers Organisation.

Eggs and poultry

There are approximately 200000 laying hens (2009) in Iceland. Most of the production is concentrated in 12 holdings. The production of eggs is 3024 tonnes per year (2009). 4.6 million birds were slaughtered in 2009, including a small number of turkeys and ducks, producing 7146 tonnes of meat and reaching 95.5% self-sufficiency. EU quality standards and labelling rules are

not applied. Apart from import protection through tariffs there are no particular support measures in the eggs and poultry sector.

Honey

There is no commercial production of honey. No market measures are applied. However, Council Directive 2001/110/EC relating to honey, has been transposed into Icelandic law.

Carcass classification and price reporting

Classification provides the basis for transparent price reporting. Rules for classification of carcasses apply to sheep, cattle, swine and horses. The use of them is compulsory. The carcass classification in line with EU requirements was adopted for sheep in 1998. For carcasses of other species Iceland applies a classification system based on national rules. Iceland stated that prices are, however, not collected systematically by the administration but surveys are made regularly.

II.a.3 Specialised crops

Support for production of **fruit and vegetables** is regulated by Regulation No. 4/2011 concerning direct payments in horticulture and the Agreement on horticultural production from 2002 which expires in 2013. Due to climatic conditions only a limited number of crops are grown on free land, mainly potatoes and other root vegetables, as well as cabbage. Greenhouses make use of geothermal energy and produce a variety of crops such as tomatoes, cucumbers and sweet peppers.

Direct payments (239 million ISK in the 2011 budget) are granted for tomatoes, cucumbers and sweet peppers and are directly coupled to production. A subsidy is given to distribution of electricity (213 million ISK budgeted in 2011). There is no aid for processing.

No producer organisations have been set up in Iceland in line with the EU model so far and there are no controls and checks to ensure compliance with marketing standards for fresh fruit and vegetables.

Directives on fruit juices and jams have been implemented through the EEA agreement.

As regards the **flowers and plants** sector, Iceland has a production of cut flowers, garden and forest plants and pot plant nurseries as well as a production of forest tree seedlings. Quality standards are not in general use except when defined in calls for tenders for seedling production. The state provides support for distribution of electricity for the use of artificial light for the production of cut flowers and pot plants in greenhouses.

There is no commercial production of **wine** in Iceland. Iceland has one, privately owned distillery for **spirits**, redistilling imported spirit. Production is almost exclusively vodka type products (vodka, spiced vodka or vodka shots). Iceland stated that labelling requirements are laid down in Iceland's Regulation No. 503/2005 on labelling of foodstuffs, which implements Directive 2000/13/EC in line with the *acquis*.

Iceland's legislation has not taken over EU rules for labelling of **olive oil**. As 99% of the imports of olive oil come from the EU, EU labelling rules are the effective market standard.

There is no production of **tobacco** in Iceland and no measures are in place related to agricultural policy.

There is no production of **seeds** for agricultural purposes in Iceland and no particular measures are in place. All agricultural and vegetable seed is imported from EEA countries as certified seed.

The Icelandic delegation stated that Regulation (IS) No. 798/2002 concerning vegetable fats other than cocoa butter that may be added to **chocolate products** is identical to Annex II to EC Directive 2000/36.

There is no production of **hops** in Iceland. There are no restrictions or specific requirements for hops in Icelandic legislation.

II.b. Rural development

Iceland has no comprehensive rural development policy.

Iceland has a few rural development 'type' measures, primarily formulated as ad hoc projects and falling under the competence of different institutions. As a consequence the schemes/projects are implemented under different management and control systems. All farms in Iceland are eligible but due to the limited budget allocated the Icelandic territory is not covered in a comprehensive way. Of the funds available, the majority is spent on extension services, afforestation and soil erosion.

Rural development 'type' measures can be found in:

- The three Agreements for, respectively, dairy (certain decoupled support), sheep (special regional support and new entrants scheme) and horticulture (improved marketing, research and education).
- The Act on Agriculture 70/1998 which aims at promoting development and increased competitiveness of agriculture as well as diversification and development of production methods. The agreed amount for 2011 is 415 million ISK (€ 2.6 million). The Act foresees that a 5 year agreement shall be negotiated with the Farmers Association based on an annual contribution from the state budget. The Farmers Association supervises all projects and programmes implemented under the Act. Participation in the measures requires private co-financing as well as payment of a service fee where applicable.

The main measures foreseen by the Act on Agriculture are: extension services, livestock breeding, development projects and the Agricultural Productivity Fund. Extension services take up more than 70% of these measures.

The development projects cover: conversion to organic farming, geothermal projects in horticulture, grain cultivation, grazing control and land use, environmental efforts, land drainage and calcium spreading on fields.

The Agricultural Productivity Fund (148 million ISK in 2010, 15 million ISK in 2011) covers education and advisory services, research, development of different farming activities, marketing, processing and forestry support. The development of different farming activities takes up 80% of this fund.

In addition, the Regional Afforestation Act No. 95/2006 aims at supporting the development of forest resources in Iceland and maintaining employment in rural areas. The grant covers 97% of

establishment costs and so far has 700 active participants under a 40 year contract. The budget for 2010 was 425 million ISK and falls under the responsibility of the Ministry of Agriculture.

Support is also provided under the Soil Conservation Act No. 17/2002. This provides a framework for the "Farmers heal the land" programme (91 million ISK) and the Land Improvement Fund (31 million ISK), both of which are designed to address the problem of soil erosion. 2/3 public co-financing of projects is required. Responsibility for the soil conservation services lies with the Ministry of Environment.

The Prevention of Riverine Erosion Act No. 91/2002 provides direct grants to land owners. Co-financing depends on the specificities of each project. The budget for 2010 was 148 million ISK.

II.c. Quality policy

Iceland has no specific legislation concerning geographical or traditional indications although some general principles are covered by the Trademark Law or the Act on surveillance of unfair business practices and market transparency. Iceland considers requesting that specific national products be registered as geographical or traditional indications.

II.d. Organic farming

Organic farming in Iceland makes for less than 1% of total agricultural production and about 2% of the food market. The Food and Veterinary Authority (MAST) is, on behalf of the Ministry of Fisheries and Agriculture, the competent body as regards organic farming. The Inspection and Certification Body, Vottunarsstofan Tún ehf., undertakes inspections and is accredited to certify organic producers and processors.

Organic farming is covered by the EEA agreement and Iceland stated that the *acquis* has been transposed into Icelandic legislation. New provisions applicable from 2009 introduced by Council Regulation (EC) No. 834/2007 as well as Commission Regulations (EC) No 889/2008 on organic production and labelling of organic products and by Commission Regulations (EC) No 1235/2008 on imports of organic products from third countries have not been implemented yet as this has not yet been included in the EEA. For instance the 'old' logo is still used in Iceland.

Iceland indicated certain reservations as regards the applicability of these new provisions due to special conditions in Iceland:

- Iceland allows to accept slatted floors in sheep houses on the ground that natural bedding materials are not available in sufficient quantities and would have to be imported at substantial cost.
- Iceland allows the feeding of ruminants with fishmeal and fish oil on the basis of tradition and because Icelandic farmers cannot grow protein crops.
- The minimum surface areas applicable to organic livestock are different from the EU ones, because traditional Icelandic breeds are smaller and lighter.
- The EU maximum stocking density for organic aquaculture would not be applicable to arctic charr.

Iceland indicated that these issues may be included in Iceland's negotiating position.

III. ASSESSMENT OF THE DEGREE OF ALIGNMENT AND IMPLEMENTING CAPACITY

III.a. Horizontal

Agricultural policy in Iceland includes a variety of measures to support agricultural producers. Overall, these schemes, as regards institutional organisation and control, differ substantially from the rules and requirements under the Common Agricultural Policy.

By Iceland's accession to the EU, the application and enforcement of the *acquis* on agriculture and rural development will need to be ensured. This will in particular require that Iceland applies EU rules on direct payment schemes and ensures the implementation of the common market organisation for various agricultural products. This will require substantial adaptation of existing legislation and of administrative structures.

Iceland has not provided indications regarding time plans for its policy-related, legislative and institutional preparations. Such plans are however an indispensable basis for negotiations on this chapter in order to ascertain that the necessary adaptations will be made in a timely manner and in accordance with the Negotiation Framework, in particular with a view to Iceland's position not to make changes in its policy, administration or its legislation until the Accession Treaty has been accepted in a referendum in Iceland. It would therefore be imperative to ask Iceland to present a strategy and an indicative time plan that demonstrate how all EU requirements will be met upon accession.

Particular efforts will be required to establish a paying agency and the necessary management and control systems that comply with the detailed requirements of the *acquis*, in particular the Integrated Administration and Control System (IACS) under which all direct payments to farmers are administered. As the administrative capacity of Iceland in the field of agriculture is relatively limited it should be examined how the institutional structures can be established in a way that makes the best use of available administrative resources, taking into account that the range of agricultural products in Iceland is narrow and that the number of farmers is relatively small. It should, however, be ensured that the administrative structures and procedures are appropriate and ensure the correct application of EU rules and correct spending of the funds.

Particular attention will need to be given to the EU requirements regarding the Land Parcel Identification System (a part of IACS). Although Iceland has a well-established cadastre system that indicates land ownership, a digitised system that indicates the borders, size and land cover of reference parcels (or equivalent) does not exist. It will need to be examined how such a system could be best applied given the specificities of the agricultural landscape and the Icelandic agriculture with emphasis on extensive mountain grazing.

For the financial management of agricultural EU expenditure, the organisational entities of the institutional framework set by the *acquis* will need to be established before accession. According to the principle of shared management, paying agencies play a central role in the management of CAP expenditure. The paying agency of a Member State needs to comply with the EU accreditation criteria irrespective of its size and/or the tasks to be carried out. The delegation of a paying agency's tasks and functions is possible under certain conditions, with the exception of the payment of EU aid. The Farmers Association is currently involved in various administrative functions in respect of executing agricultural policy in Iceland, such as managing databases of the support schemes, calculating entitlements and checking and executing payments to beneficiaries. This set-up will need to be analysed and brought into line with the *acquis* by accession.

Iceland's system to collect farm accountancy information is substantially different from what is required for the correct implementation of the Farm Accountancy Data Network, for instance as regards community typology and farm classification, physical and structural data, the sample and selection of the returning holdings as well as the procedures for the collection of the information.

As regards **State aid**, agriculture is excluded from the scope of the EEA Agreement. For this reason the legal base on state aid measures in agriculture will have to be analysed further in view of bringing it into line with the EU *acquis*.

III.b. Common market organisation

Iceland does not produce many agricultural products compared to the EU and hence has no rules for those products. It will need to be able to apply the complete set of market mechanisms of the EU *acquis* upon accession, including intervention stocks. Iceland is not applying export refunds but will have to establish required trade measures (e.g. certificates, customs controls) in case Iceland would become a transport hub for certain products.

III.b.1 Arable crops, fibre, sugar

Arable crops play a limited role in Iceland. The coupled payment for barley production is not in line with EU rules.

III.b.2 Livestock products

The existing system of coupled direct payments in the livestock sector is not in compliance with EU rules as regards the dairy sector and the payments for cattle and partly for sheep. This does not concern the other meat sectors with no direct payments such as pig meat and poultry and eggs.

In the milk sector the system of minimum producer prices and the price transferral levy are not in compliance with EU rules. The milk quota system in Iceland differs from the EU milk quota system. It should be taken into account that the EU's milk quota system is not expected to continue after 2015.

Iceland will need to ensure compliance with EU rules for carcass classification and price reporting.

III.b.3 Specialised crops

As regards **fruit and vegetables**, the system of coupled direct payments for certain vegetables is not in compliance with EU rules. The subsidy given for distribution of electricity for greenhouses would need to be assessed.

Under the *acquis*, the setting up of producer organisations is not obligatory and is left up to the initiative of producers. Iceland will however have to implement all other provisions of the single Common Market Organisation and its implementing rules pertaining to fruit and vegetables by accession. This in particular applies to marketing standards requirements for fresh fruit and vegetables at all marketing stages (wholesale, import, export etc.), and to perform conformity checks in line with requirements of the EU *acquis* (trader database, risk analysis etc).

Furthermore, Iceland will need to apply and monitor the relevant provisions of EU olive oil legislation. In this context Iceland will have an exclusive competence to take the necessary control measures at national level, including the system of penalties, to ensure compliance with the EU acquis and to address the risks represented by the adulteration of olive oils.

III.c. Rural development

Iceland does not have a coherent and comprehensive rural development policy. It has experience with some measures and activities that could fall within the scope of rural development policy. However, strategies and methodological approach to priority setting, programming and implementation is lacking.

For Iceland to become part of the Common Agricultural Policy, a coherent and comprehensive rural development strategy and programme will have to be developed; management and control systems will have to be established, including a Paying Agency in accordance with EU requirements. The paying agency responsible for direct payments and market support can also be responsible for rural development measures.

III.d. Quality policy

Iceland has not taken over the acquis for quality policy.

III.e. Organic farming

Iceland has taken over the acquis in the field of organic farming as a member of the EEA. The implementation of the recent regulation (EC) No. 834/2007 on organic production and labelling of organic products and of Commission Regulations (EC) No 889/2008 and 1235/2008 has however not been implemented for the non-EU members of the EEA. Irrespective of EEA procedures Iceland must, in the context of EU accession, ensure that all EU acquis is fully taken over by the day of accession at the latest.

The particular requests regarding organic farming that Iceland may include in its negotiation position must be assessed in detail during the accession negotiations on this chapter.