IV. TRADE POLICIES BY SECTOR

(1) OVERVIEW

1. Agriculture contributes a small and dwindling share to total GDP and employment in Iceland. The OECD estimates that the Producer Subsidy Equivalent has fallen but still stands at more than twice the OECD average. Support to the agriculture sector is provided through both internal and border measures. Milk production is supported through production-linked direct payments and is subject to production quotas and administered prices. Sheep meat production is supported through direct payments based on support targets and through quality-dependent payments; exports of lamb meat are regulated to control domestic supply. Direct payments are also provided to producers of certain vegetables. The average MFN applied tariff for agricultural products (18.3%) is many times higher than for other products (see Chapter III). Tariff quotas apply in practice to some 86 tariff lines, with out-of-quota rates ranging up to 306%. When demand exceeds available in-quota volumes for minimum access commitments, quotas are auctioned. As at early 2006, quotas are not assigned to particular countries but from 2007 a reciprocal quota system will come into operation with the European Union.

2. Although its share in GDP has continued to decrease, reflecting the diversification of Iceland's economy, the fishing industry remains of crucial importance, contributing 60% of total merchandise export revenues. To protect the resource base, the volume of annual catch is managed through a system of transferable individual fishing quotas. Since 2004, a fee is collected on holders of harvesting rights. Ownership of fishing operations and primary fish processing is limited to Icelandic nationals or residents, although non-residents can own up to 25% of the shares in Icelandic companies involved in these activities.

3. Iceland is also richly endowed with energy resources, and energy costs are low by international standards. Almost all electricity generated stems from hydro and geothermal energy. There have been important legislative changes in the energy sector designed to promote greater efficiency and competition, driven by Iceland's EEA obligations. However, the electricity industry remains entirely owned by the State or local governments. Only Icelandic, EEA or EFTA residents and legal entities may own energy exploitation rights or enterprises involved in producing or distributing energy, although agreements may be reached to extend these benefits to other parties.

4. The manufacturing sector is concentrated mainly in power-intensive industries although other industries have gained in importance. The sector is export-oriented, given the small size of the domestic market; it accounts for some 35% of total merchandise exports (aluminium alone contributes 18%). Manufactured exports have expanded significantly over the review period and the development of power-intensive industries has continued to be the source of significant inflows of foreign direct investment.

5. The services sector has continued to expand since Iceland's last Review and now generates just over 80% of GDP. Under the GATS, Iceland undertook sector-specific commitments in 9 of the 12 sectors included in the Agreement. It also signed the Fourth Protocol on Basic Telecommunications and adopted the principles set forth in Reference Paper. On financial services, Iceland's commitments cover the full spectrum of activities, and are in accordance with the Understanding on Commitments on Financial Services.

6. The current structure of the financial sector is the result of a process of privatization and intense consolidation between 1998 and 2003. A state-owned firm (the Housing Financing Fund) remains the largest institution in the financial system. There is one branch of a foreign bank operating

in Iceland, but no subsidiaries or representative offices. In contrast, Icelandic banks have made significant international acquisitions recently and, partly as a result, half of the assets of the three major banks are held by their foreign subsidiaries. Iceland's insurance market is characterized by a relatively high degree of concentration. Financial services legislation has undergone extensive revisions since Iceland's last Review. Iceland's banking and insurance markets are largely open to foreign participation, although treatment of foreign firms differs markedly between EEA-licensed firms and other firms. Thus, for example, in insurance, non-EEA-licensed companies may not set up branches in Iceland unless their home countries grant reciprocal treatment to Icelandic companies. The cross-border provision of insurance services is limited to EEA insurance companies.

7. The Icelandic telecommunications sector has undergone major change since 1998 with the separation of postal from telephone services, the privatization of Iceland Telecom, the opening up of the sector to competition, the entry of new firms, and company consolidation within the sector. There has also been a series of legislative changes, largely driven by EEA membership requirements. As a result of those changes, natural persons and legal entities established within the EEA and within WTO Members do not need a permit to start operation unless specific frequencies are involved.

8. Due to Iceland's geographical location and its reliance on international trade, maritime, and air transport play a major role in its economy. With respect to passenger transport to and from Iceland, Icelandair has a dominant position. There are restrictions to foreign participation in the air transport sector: foreign ownership in Icelandic companies involved in airline operations may not exceed 49%. During the review period, Iceland signed new bilateral air transport agreements with five trading partners outside the EEA, and one memorandum of understanding.

9. Practically all movements of goods and materials to and from Iceland are by maritime transport. There are no restrictions on private or foreign ownership of ports, however, all ports are currently the property of the community in which they are located. New legislation has been adopted over the review period and as a result, ports are now free to set their own fees. Legislation was also adopted against terrorist threats or other illegal activities. Iceland participated in the Extended Negotiations on Maritime Transport Services, suspended in 1996. Although most participants withdrew their conditional offers, Iceland requested that its offer be made an integral part of its GATS Schedule of Specific Commitments.

(2) AGRICULTURE

(i) Main features

10. The agriculture sector contributed an estimated 1.4% to GDP in 2004[1], down from 2% in 1998 and 5% in 1980. The sector employed 5,207 people, around 2.7% of the total work force, again, a reduction on the figures reported in Iceland's previous Review.

11. As reported by the Central Bank of Iceland, around one-fifth of Iceland's total land area is suitable for fodder production and the raising of livestock. Around 6% of this area is cultivated; the rest is used to raise livestock or remains undeveloped.[2] The authorities stress that agricultural support is in part intended to keep the Icelandic countryside populated, with greatest support and protection being afforded to a few sensitive products, and that there has been a gradual move to greater openness in the sector in recent years.

[1] Central Bank of Iceland (2005a).
[2] Central Bank of Iceland (2005a).

12. The main agricultural activities in Iceland are cattle and sheep farming, which account for some two thirds of the value of agriculture output.[3] The principal crops grown are hay, potatoes, and, more recently, cereal grains. Since the mid-1980s there has been diversification into various fruit, flowers, vegetables, and other plants, which are cultivated in greenhouses heated by geothermal water and steam. Table IV.1 provides details of agricultural production in Iceland over the review period.

Table IV.1
Production of main crops and meat, 2000-04
(Tonnes, unless otherwise indicated)

Production	2000	2001	2002	2003	2004
Field crops					
Total hay yield (m^3)	2,363,342	2,391,067	2,175,427	2,287,936	1,895,593
Potatoes	9,843	11,366	8,800	7,090	..
Turnips	795	730	..	959	666
Carrots	179	296	302	347	374
Cereal grains	3,041	4,337	..	4,337	10,255
Tomatoes	931	964	948	1,074	1,318
Cucumber	831	1,049	..	896	930
Cauliflower	89	84	80	71	83
Cabbage	538	503	558	555	380
Peppers	203	195	..	79	97
Chinese cabbage	255	253	..	269	203
Mushroom	447	450	..	465	461
Meat					
Mutton and lamb	9,735	8,616	8,676	8,792	8,644
Beef	3,626	3,683	3,639	3,624	3,611
Horse meat	1,100	1,055	1,019	912	883
Pork	4,783	5,284	6,011	6,205	5,597
Poultry	3,051	3,776	4,633	5,706	5,392

.. Not available.

Source: Statistics Iceland online information. Available at: http://www.statice.is.

13. Iceland is a net importer of agricultural products, mainly those with no domestic substitutes. According to Comtrade data, in 2004, Iceland's most significant exports in value terms were live horses (US$9 million) and sheep meat (US$8.4 million).

14. Agriculture in Iceland falls under the responsibility of the Minister of Agriculture. A number of subsidiary bodies report to the Minister. In 2005, a law was passed (Law No. 80/2005) authorizing the creation of the Agricultural Authority of Iceland, which began operations on 1 January 2006. The Authority *inter alia* has a monitoring role and gives guidance to the Ministry of Agriculture in all areas concerning the health and safety of agricultural production. The Authority has taken over the functions of the Chief Veterinary Officer, the Directorate of Freshwater Fisheries, the Meat Classification Board, the Plant Protection Service, and the Feed, Seed and Fertiliser Inspectorate. In addition the Authority has taken over some of the administrative duties formerly carried out by the Farmers' Association and the Plant Protection Service from the Agricultural University of Iceland.

15. The Farmers' Association continues to provide advisory services to farmers in all spheres of agriculture and participate in policy making as well as to provide information to Government and public authorities. The Agricultural University of Iceland was founded in 2005 as a result of a merger between the Agricultural University of Hvanneyri, the Horticultural College of Reykir and the Agricultural Research Institute. A second agricultural research and teaching facility at university level is operated at Holar in north Iceland.

[3] Farmers Association of Iceland (2005).

16. Act No. 99/1993 on the production, pricing and sale of agricultural products remains the main legislative framework defining Iceland's agricultural policy. The policy's main stated objectives are to promote structural adjustment and increased efficiency in agricultural production and processing; to guarantee at all times sufficient supply of agricultural products; to ensure that the income of farmers will be equitable with the earnings of other comparable occupations; and to integrate environmental issues with agricultural policies. Changes to the Act during the review period have focused on improving the quality of agricultural produce (Act No. 101/2002), and creating a price equalization mechanism to support agricultural exports (Act No. 82/2003). In addition, Act No. 84/2002 authorizes direct payments to farmers producing vegetables and plants in greenhouses (see section (iii)) and Act No. 61/2004 stipulates new rules regarding the production of milk (see section (iii)).

(ii) General support schemes

17. Support to the agricultural sector is provided through both internal and border measures. As reported by the Central Bank of Iceland, Icelandic agriculture is the most heavily supported in the world.[4] The vast majority of this support is for the sheep and dairy segments and takes the form of direct payments to farmers based on support targets (negotiated between the Minister of Agriculture and the Farmers Union). Support to producers as measured by the % PSE, is estimated at more than twice the OECD average, though it has fallen from 77% in the 1986-88 period to 70% over the period under review.[5]

18. Iceland notified to the WTO its domestic support commitments since the beginning of the Uruguay Round implementation period, most recently a notification covering the years 2001, 2002 and 2003.[6] For 2003, Iceland's total AMS commitment level for the period was SDR 130.1 million and total AMS for the period was SDR 123.6 million (inflation adjusted).

19. Internal measures include various funds, in particular the Agricultural Productivity Fund (APF) and the Agricultural Loan Fund (ALF). In October 2005, the Icelandic Government sold the ALF to Landsbanki Bank. The fund has ceased to exist in its original form and has been incorporated into the bank's activities.[7]

20. The Agricultural Productivity Fund (Law 89/1966) grants subsidies and loans to facilitate increased productivity in agriculture and business activities in farms, as well as providing capital to strengthen new branches of agriculture, reorganize activities, and support projects undertaken in rural areas to create alternative employment. The fund's income comes from the Ministry of Agriculture and, from customs duties levied on imported animal feeding stuffs. In 2004 income amounted to ISK 235 million and the APF paid out ISK 205.2 million.[8]

21. In 2003, the most recent year for which information was available, other "green box" forms of assistance totalled ISK 4.320 billion. This comprised: general services to farmers (general research; product particular research; pest and disease control; extension and advisory services; and marketing and promotional services) (ISK 1.128 billion); stockholding costs; sheep meat programme (ISK 260.1 million); direct payments to sheep meat farmers (ISK 2.034 billion); livestock compensation payments (ISK 42.7 million) and financial and physical restructuring programmes due

[4] Central Bank of Iceland (2005a).

[5] OECD online information. Available at: http://www.oecd.org/dataoecd/34/10/35331600.pdf.

[6] WTO document G/AG/N/ISL/26, 16 December 2005.

[7] Ministry of Agriculture online information. Available at: http://www.landbunadarraduneyti.is/frettir/frettatilkynningar/nr/758.

[8] The Agricultural Productivity Fund online information. Available at: http://www.fl.is.

to structural disadvantages; permanent withdrawal of sheep meat production entitlements; farmer pension fund (retirements schemes) (ISK 449.2 million); and environmental and afforestation programmes (ISK 405.7 million).[9]

22. In its most recent notification on the subject, Iceland notified the WTO that it did not provide export subsidies in the calendar years 2000, 2001, and 2002.[10]

(iii) Support for dairy, sheep, and vegetable production

23. A new agreement governing milk production through to 2012 took effect on 1 September 2005 (Act No. 61/2004 changing Act No. 99/1993). The agreement continues the system of production quotas for dairy farms. The production quota for each dairy farm is a specific share of the production quota for the whole country, which is based on sales in the previous year. Farm production quotas can be transferred and sold. In 2004/05 the production quota for the country was 106 million litres. For 2005/06 the quota was increased to 111 million litres (Regulation 620/2005). The Ministry of Agriculture determines the farm quota and in this regard is advised by the Farmers' Association. Direct payments in 2005/06 are set at ISK 3.9 billion. During the agreement period state expenditure is to be reduced by 1% each year.[11]

24. The Agricultural Pricing Committee (Verdlagsnefnd Buvara) sets a minimum producer price for milk each year, and regularly sets the wholesale price for a number of dairy products. The legislation provides for the possible abolition of administered prices at any time by decision of the competent authorities.

25. Act No. 85/2004 states that dairy processing plants can cooperate to bring down the costs of production, storage, and distribution notwithstanding the prohibition against such cooperation in the Competition Law (Act No. 44/2005) (see also Chapter III(4)(ii)).

26. In 2001, an agreement on sheep meat production through to 2007 was reached (Act No. 88/2000 amending Act. No. 99/1993). Support to farmers is mainly in two forms. Firstly, farmers receive a direct payment based on the farm's support target as registered for each farm by the Farmer's Association, using production in the year 2000 as a base year. This support target is not related to the actual level of production. Rather it stipulates the right to a certain amount of direct payments, hence, farmers can receive full payment irrespective of their level of production. In 2004, approximately 1,500 sheep farmers qualified for direct payments, which in 2006 are estimated at ISK 1.6 billion. Secondly, farmers who fulfill the criteria for quality controlled production (set out in Act No. 101/2002 and Regulation No. 175/2004) can receive a special payment. In 2006, such payments are estimated to be ISK 552 million. The agreement (Act No. 88/2000 amending Act No. 99/1993) also puts forward plans by the Government to buy up certain amounts of support targets from farmers at set prices.[12] These plans were implemented shortly after the Agreement entered into force. Administered wholesale and producer prices were abolished in 1995 and 1998

[9] WTO document G/AG/N/ISL/26, 16 December 2005; Budget 2005.

[10] WTO document G/AG/N/ISL/22, 29 April 2003.

[11] Farmers' Association of Iceland (2005); and Minisry of Agriculture online information. Available at: http://www3.landbunadarraduneyti.is/upplysingar/bunadarmal/nr/532.

[12] Ministry of Agriculture online information. Available at: http://www3.landbunadarraduneyti.is/upplysingar/bunadarmal/nr/310.

respectively. The Association of Sheep Meat Producers puts forward a list of recommended prices every year.[13]

27. Producers of lamb meat, are obliged to export a certain percentage of their annual production, in order to regulate the domestic supply of lamb. This regime is governed by the Law on the Production, Pricing and Sale of Agricultural Products (No. 99/1993), and is implemented by Regulation No. 524/1998. Each year, the Ministry of Agriculture advertises the percentage of domestic supply of lamb meat that is to be exported, based upon recommendations from the Farmer's Association. The export levels set for the most recent five slaughter periods are: up to 18% (2005/06); up to 36% (2004/05); up to 38% (2003/04); 25% (2002/03) and 10% (2001/02). If slaughterhouses do not export the required percentages of domestically produced lamb meat, they must pay penalty fees equal to the difference between local and export prices.[14]

28. In 2002, an agreement was reached between the Ministry of Agriculture and vegetable producers (Act No. 84/2002 changing Act No. 99/1993) providing for direct payments to farmers producing tomatoes, cucumbers, and peppers. According to the authorities, this was aimed at providing production-linked support for these producers when duty free importation of these products was allowed. Regulation 1080/2005 sets the level of support for 2006 at ISK 201 million. The support will be paid out to farmers in accordance with the types of vegetables produced and amounts sold.

(iv) Tariffs and tariff quotas

29. The average MFN applied tariff for agriculture (ISIC definition) in 2005 was 18.3% (Table III.2). As a result of the Uruguay Round, 100% of Iceland's agricultural tariff lines are bound, up from 58% at the time of Iceland's first Trade Policy Review in 1994. Average bound rates remain well above applied duties; the average final bound rate is 120.5%.

30. Iceland reserved the right to use tariff quotas that were submitted in the Schedule LXII-Iceland (bound tariff quotas), and later transposed to the HS96 classification, which became effective on 27 January 2003.[15] A total of 528 goods (tariff lines) are subject to bound quotas in the HS96 classification, on which Iceland made minimum or current access commitments under the WTO Agreement on Agriculture. Of these, 396 are subject to *ad valorem* duties and 132 are subject to compound duties (mainly minimum access commitments). For a number of lines the quota regime has not been applied, and only applied rates of duty equal to, or lower than, the corresponding in-quota rates have been used.

31. In practice, only 86 goods (at the eight-digit level) were subject to tariff quotas in 2005 (Table IV.2). Out-of-quota duties were all compound rates. The specific part of the duties ranged from ISK 52/kg. to ISK 1,462/kg. In-quota rates were all compound, except for two lines with *ad valorem* rates; all the compound rates had duty-free *ad valorem* components and specific components ranging from ISK 26/kg. up to ISK 576/kg.

32. Quota allocations to importers are made by the Minister of Agriculture based on recommendations made by a special committee comprising representatives from the Ministries of Agriculture, Commerce, and Finance. The Regulations outlining the different tariff quotas are

[13] The Farmers' Association of Iceland online information. Available at: http://www.bondi.is/landbunadur/wgbi.nsf/key2/vstr6djfhx.html.

[14] Ministry of Agriculture online information. Available at: http://www.landbunadarraduneyti.is.

[15] WTO document WT/Let/477 18 October 2004, Certification of modifications and rectifications to Schedule LXII – Iceland.

accessible online.[16] If applications exceed the available quota, allocations are auctioned, and quotas are always allocated to the highest bidder. The bidding process effectively results in additional import charges. For example, in June 2005 twelve bids were received for the import of 345,000 kg. of poultry while the quota available amounted to only 59,000 kg. Six bids were accepted at an average price of 393 ISK/kg.[17]

33. As at early 2006, quotas are not assigned to particular countries. From 2007, however, a reciprocal quota system will be in operation with the European Union.

Table IV.2
Products subject to tariff quotas 1 July 2004-30 June 2005

Description	Out of quota tariff	In-quota rate (%)	In quota rate (ISK/kg.	Final tariff quota (Period 07.04-06.05)	Fill rate (%)
Beef meat[a]					
0202.3, 0210.2001	30% + (ISK 510 to 1,462/kg.)	0	547; 333	95,000	57
Pork[a]					
0203.29, 0210.1200, 0210.1901, 0210.1909	30% + (ISK 361 to 1,462/kg.)	0	443; 317 360; 360	64,000	17.5
Poultry[a]					
0207.1, 0207.2, 0207.3	30 % + (ISK 439 to 900/kg.), 30% + (ISK 499 to 1,000/kg.), 30% + (ISK 256-1,000/kg.)	0	163; 224 224	59,000	216.6
Other meat[a]					
0208.9007, 0208.9008	30% + (ISK 1,014/kg.)	0	515	9,000	..
Processed meat[b]		0			
1602.1001, 1602.1009, 1602.2011, 1602.2012, 1602.2019, 1602.2021, 1602.2022, 1602.2029, 1602.3101, 1602.3102, 1602.3109, 1602.3201, 1602.3202, 1602.3209, 1602.3901, 1602.3902, 1602.3909, 1602.4101, 1602.4102, 1602.4109, 1602.4201, 1602.4202, 1602.4209, 1602.4901, 1602.4902, 1602.4909, 1602.5001, 1602.5002, 1602.5009, 1602.9011, 1602.9012, 1602.9019, 1602.9021, 1602.9022, 1602.9029	30% + (ISK 177 to 1,144/kg.)	0	92; 92; 129 129; 44; 129 78; 26; 224 224; 115 224; 224 115; 224 224; 115 576; 343 115; 412 247; 83 511; 307 102; 400 304; 102 442; 265 89; 442 265; 89	86.000	90.2
Butter[c]					
0405	30% + (ISK 220 to 623/kg.)	0	220	53,000	0

Table IV.2 (cont'd)

[16] Ministry of Agriculture online information. Available at: http://www.landbunadarraduneyti.is/upplysingar/flutningur-buvara/tollkvotar/.

[17] Ministry of Agriculture online information Uthlutun tollkvota i juni 2005. Available at: http://www.landbunadarraduneyti.is/upplysingar/flutningur-buvara/tollkvotar/nr/663.

Description	**Out of quota tariff**	**In-quota rate (%)**	**In quota rate (ISK/kg.**	**Final tariff quota (Period 07.04-06.05)**	**Fill rate (%)**
Cheese[c]					
0406.1000, 0406.2000, 0406.3000, 0406.4000, 0406.9000	30% + (ISK 430 to 500/kg.)	0	156; 156 117; 179 175	119,000	141
Potted plants not exceeding 1m in height; fresh flowers[d]					
0602.9095, 0603.1009	30% + ISK 95/item 30% + ISK 200/item	30	0	2,500; 125,000 (period 07.04-12.04)	..

.. Not available.

a Regulation 403/2004.
b Regulation 401/2004.
c Regulation 402/2004.
d Regulation 400/2004.

Source: Ministry of Agriculture Regulations 400, 401, 402, 403/2004; and WTO document G/AG/N/ISL/25.

(v) Other border measures

34. Import licensing and other restrictions affect a number of agricultural products, including: live animals; animal products and products capable of containing infectious agents that are deemed dangerous to animal and human health; as well as feeds, seeds and plant products (Chapter III(vi)). In addition, a number of conditions attached to certain imports of human and pet food containing meat require certificates to be provided.[18]

35. Iceland has reserved its right to use the special safeguard provisions of the Agreement on Agriculture for all products subject to tariff quotas. However, Iceland has reported that it has not invoked these provisions to date.[19]

(vi) Internal taxation

36. Iceland applies a number of taxes on agricultural products as well as levies at producer level as shown in Table IV.3.

Table IV.3
Treasury income derived from taxes and fees applied on agricultural activities, 2004
(ISK million)

Source and type of tax	**Taxes raised**
Agricultural Institute	
Feed inspection tax: charged at 0.9% of the c.i.f. price of feed and 0.17% of the c.i.f. price of fishmeal and cod liver oil, both imported and domestic; used to pay for inspections by the Agricultural Institute (Regulation 340/2001)	19
Agricultural University (formerly Agricultural Research Institute)	
Import inspection tax on plants, earth and fertilizer: amounts to 1-2% of the c.i.f. price depending on the product	15

Table IV.3 (cont'd)

[18] Regulation 509/2004 on measures to prevent the introduction of animal diseases and contaminated products in Iceland, Chapter III.
[19] WTO documents G/AG/N/ISL/3, 17 October 1996; G/AG/N/ISL/7, 15 July 1997; G/AG/N/ISL/13, 26 January 1999; G/AG/N/ISL/18, 23 February 2001; G/AG/N/ISL/21, 30 October 2002; G/AG/N/ISL/23, 29 July 2003.

Source and type of tax	Taxes raised
Agricultural Productivity Fund	
Feed tax: charged at ISK 0.80 per kg. of imported raw material and ISK 7.80 per kg. of imported whole feed compounds. The tax is refunded in full to salmon and fur farmers and in part to the other agricultural subsectors (Act No. 87/1995 and Regulation 431/1996). The remainder of the income from the feed tax goes to the Agricultural Productivity Fund to dispose of in the form of loans and grants to agricultural projects. In 2004 the APF received ISK 50 million	50
Other taxes and charges	
State farm property rent	39
Levy on farm income: charged at 2% of farms' total agricultural income (Law 84/1997 amended by Law No. 59/2002). As of 1 January 2006, this will be reduced to 1.2%. The collection and distribution of the levy is administered by the Farmer's Association, and divided between a number of institutions including the Agricultural Loan Fund	400

Source: Budget 2005, Agricultural Productivity Fund (2003 and 2004), *Annual Report*; Agricultural Loan Fund (2003 and 2004) *Annual Report*; Regulation 110/1992, Regulation 340/2001: Change 13, Act No. 87/1995; and Act No. 59/2002.

(3) FISHERIES AND FISH PROCESSING

(i) Main features

37. Fisheries remains Iceland's most important economic activity. In 2004, fishing and fish processing accounted for some 8.7% of GDP and 60% of total merchandize export revenue, down from 71% in 1998 and around 90% in the early 1960s.[20] Some 9,900 people are employed directly in fishing or fish processing activities, of which 4,500 are fishermen.[21] The main species fished in Icelandic waters are cod, haddock, saithe, redfish, halibut, herring, capelin, and blue whiting.[22] Cod is the most important species in economic terms, accounting for 41% of the total catch value in Icelandic waters in 2004.[23] The registered Icelandic fishing fleet totalled 1,824 vessels in 2004, of which 1,614 fishing vessels were active.[24]

38. Exports of marine products were valued at ISK 121.7 billion in 2004, from a total catch of about 1.7 million tonnes. Some 97% of the total catch is exported. The majority of Icelandic fisheries products are exported to the EU, particularly the United Kingdom. Other significant export markets include the United States and Japan. In 2004, Iceland imported around 200,000 tonnes of marine products (raw material)[25], for a total value of ISK 6.5 million. Most of these imports were from vessels registered in Norway, the Faroe Islands, and Greenland, and were processed and subsequently exported.[26]

39. There has been significant merger activity among many of the larger fisheries companies over the review period as firms have sought to enhance efficiency and benefit from economies of scale. As at 1 September 2005, the ten largest fisheries companies held harvesting rights of about 46% of the total quota holdings[27]; the two largest, HB Grandi hf. and Samherji hf., held over 16%.

[20] Central Bank of Iceland (2005).
[21] Statistics Iceland online information. Available at: http://www.statice.is.
[22] Statistics Iceland online information. Available at: http://www.statice.is.
[23] Central Bank of Iceland (2005).
[24] Statistics Iceland online information. Available at: http://www.statice.is.
[25] Statistics Iceland includes as "raw material": demersal catch, flatfish catch, pelagic catch, and shellfish catch. Statistics Iceland online information. Available at: http://www.statice.is.
[26] Statistics Iceland online information. Available at: http://www.statice.is.
[27] Central Bank of Iceland (2005).

40. There have also been recent efforts to develop Iceland's aquaculture capacity. As reported by the Ministry of Fisheries, major fisheries companies have been investing in this area and are planning further expansions. Likewise, the Marine Research Institute's (MRI) research in this area, which is focused on the farming potential of halibut, cod, turbot, and abalone, has been expanded with an increase in the capacity of its mariculture laboratory located on the south-west coast of Iceland. The Ministry of Fisheries estimates that in 2009, the export value of aquaculture will be about ISK 5 billion, up from ISK 1 billion in 2001.[28]

(ii) Institutional and legal framework

41. The Ministry of Fisheries is responsible for the management of fisheries in Iceland, including determining the annual total allowable catch quotas (TAC) (Act No. 38/1990, Article 3), conservation of living marine resources, and supporting research and development in the sector.[29] The Ministry is assisted in its functions by the Directorate of Fisheries, the MRI, and the Icelandic Fisheries Laboratories (IFL). The Directorate of Fisheries is responsible for the day to day administration of living marine resources, and implementation of government policy and legislation in this area.[30] The MRI conducts research on Iceland's marine environment and provides formal advice to the Ministry of Fisheries on sustainable fishing strategies and the TAC.[31] The Icelandic Fisheries Laboratories is a research body operating under the auspices of the Ministry of Fisheries.[32]

42. In the area of aquaculture, the Ministry of Agriculture is responsible for freshwater species, the Ministry of Fisheries is responsible for marine species and the Ministry of Environment has the authority to grant operating licences.

43. The Fisheries Management Act (Act No. 38/1990 and subsequent amendments) aims to promote the conservation, and efficient and sustainable utilization of the exploitable marine stocks of the Icelandic fishing banks, and to ensure stable employment and the economic viability of fishing communities throughout the country (Article 1). The Ministry of Fisheries determines annually the TAC quota for the 25 species of fish subject to quotas, which together comprise around 95% to 97% of the total annual catch value.[33] Fixed quota shares of the TAC are allocated to individual fishing vessels based upon catch history prior to the creation of the quota system.[34] In 2004, the quota regime was fully extended to small vessels (under 15 tons).[35]

44. In fishing year 2004/05 a fishing fee on owners of vessels holding harvesting rights was introduced (Act No. 85/2002 amending Act No. 38/1990); it will be fully phased in by fishing year 2009/10. For each fishing year the fee is based on the earnings of the fishing sector as well as the allocation of the catch permit.[36] According to the authorities in the fishing year 2004/05 around ISK 1 billion was collected in fishing fees.

45. As a result of Act No. 85/2002 (amending Act No. 38/1990), individual fishing enterprises may not control more than 12% of the value of total quotas allocated for all species and up to 35% for individual species (depending on the species). Quotas are transferable, in whole or in part; however,

[28] Ministry of Fisheries (2004).
[29] Ministry of Fisheries online information. Available at: http://eng.sjavarutvegsraduneyti.is.
[30] Directorate of Fisheries online information. Available at: http://www.fiskistofa.is.
[31] Marine Research Institute online information. Available at: http://www.hafro.is.
[32] The Icelandic Fisheries Laboratories online information. Available at: http://www.rfisk.is.
[33] The fishing year runs from 1 September to 31 August.
[34] Quota shares are mainly allocated on the basis of catches of different species in the 1981-83 period.
[35] Act No. 74/2004 (amending Act No. 38/1990).
[36] Details of how the fishing fee is calculated are outlined in Ministry of Fisheries (undated).

quotas may not be traded from small vessels (as defined above) to larger ones. Quota transfer, however, is allowed from the large fishing fleet to the small. As reported by the authorities, a large share of the annual catch quota is traded each year; much of this is internal company transfers between vessels owned by the same operator. In addition, interspecies trade is common, with operators trading part of their annual catch quota in one species for a quota in another. Catch quotas are also traded for money.[37] Applications for quota transfers are made to the Directorate of Fisheries, which verifies and registers the transfer. The Minister of Fisheries may also allocate discretionary quotas for up to 12,000 tons of cod, which serve as shock absorbers and regional policy instruments (Act No. 147/2003). These discretionary quotas account for a small percentage of the total catch.

46. Ownership of fishing operations and primary fish processing[38] is limited to Icelandic citizens and to Icelandic legal persons wholly owned by Icelandic citizens or by Icelandic legal persons controlled by Icelandic residents and not more than 25% owned by foreign residents, calculated on the basis of share capital or initial capital. However, if the share of an Icelandic legal person in a legal person conducting fishing operations or fish processing in Iceland is not above 5%, the share of the foreign resident may be up to 33%. There are no restrictions on foreign ownership in secondary fish processing operations, except for those applied generally as stipulated in acts on limited liability companies.

47. In the horizontal commitments of Iceland's GATS Schedule, it is specified that investment by non-residents in fish farming may not exceed ISK 250 million within a year unless a special concession is given. In the context of the current round of trade negotiations, Iceland has made a conditional GATS offer to remove this limitation, provided that investments are reported to the Ministries of Commerce and Industry and the Central Bank of Iceland.[39]

48. Iceland supports a sectoral agreement on fish and fish products that would result in the elimination or substantial reduction of tariffs within the current round of trade negotiations, and has made a communication to this effect in conjunction with a number of other WTO Members.[40] Iceland supports the reduction of trade distorting fisheries subsidies within the current round of trade negotiations. Iceland has made two submissions, jointly with other WTO Members, on fisheries subsidies in the Negotiating Group on Rules.[41]

49. As outlined in Chapter III(4)(iii)(b), governmental support to the fisheries sector includes: the Fisheries Project Fund created in 2003[42] (this includes the assets of the Fisheries Development Fund, which was disbanded in October 2005); the Research Fund to Increase the Value of Sea Produce; grants to enhance scientific knowledge in marine aquaculture[43]; and state aid to domestic fish-processing companies to support vocational training in the fishing industry.

[37] Speech by the Permanent Secretary of the Ministry of Fisheries in Iceland, Moscow 11 September 2005 (http://eng.sjavarutvegsraduneyti.is).

[38] Includes freezing, salting, drying and any other processing which protects fish and other marine products from decay, including the production of fish-oil and fish-meal.

[39] WTO document TN/S/O/ISL/Rev.1, 14 June 2005.

[40] WTO document TN/MA/W/63, 18 October 2005. Joint communication from Canada, Iceland, New Zealand, Norway, Singapore and Thailand on "Market Access for Non-Agricultural Products: Liberalization of Trade in Fish and Fish Products".

[41] WTO document TN/RL/W/196, 22 November 2005 (joint paper from Brazil, Chile, Colombia, Ecuador, Iceland, New Zealand, Pakistan, Peru and the United States) and WTO document TN/RL/W/58, 10 February 2003 (submission from Argentina, Chile, Iceland, New Zealand, Norway and Peru).

[42] Act No. 146/2003.

[43] WTO document G/SCM/N/123/ISL, 16 November 2005.

50. The EEA Agreement does not cover fisheries, however, European rules on food safety do apply to seafood produced in Iceland. Iceland has a number of bilateral agreements in place allowing certain countries to fish in Icelandic waters.[44]

51. The Directorate of Fisheries is responsible for issuing temporary fishing permits to foreign vessels in conformity with decisions by the Ministry of Fisheries, and international fishing agreements to which Iceland is party. The authorities of countries granted fishing rights through international agreements must apply to the Directorate for fishing permits before their vessels may begin fishing (Act No. 22/1998, Art. 6). Iceland is a party to a number of international agreements and conventions.[45]

(4) OTHER MANUFACTURING

52. Manufacturing activities in Iceland are mainly concentrated in power-intensive industries based on Iceland's natural endowment of energy-generating sources. Some 16,900 people were employed in manufacturing (not including fish processing) in 2004. According to data from Statistics Iceland, the main activities by value of sales are food products and beverages (about 55% of the total) followed far behind by basic metals (14%) (Table IV.4).

Table IV.4
Manufactured products, 2004

	Value of sales (ISK million)	Per cent
Other mining and quarrying	1,475	0.5
Food products and beverages	166,644	55.1
Textiles	3,234	1.1
Wearing apparel; dressing and dyeing of fur	725.2	0.2
Wood and wood products	3,387	1.1
Pulp, paper and paper products	1,866	0.6
Publishing, printing and reproduction of recorded media	16,290	5.4
Chemicals and chemical products	15,709	5.2
Rubber and plastic products	4,818	1.6
Other non-metallic mineral products	11,012	3.6
Basic metals	42,880	14.2
Fabricated metal products, except machinery and equipment/machinery and equipment n.e.c.	19,142	6.3
Electrical machinery and apparatus n.e.c./Radio, television and communication equipment.	854	0.3
Medical, precision and optical instruments, watches and clocks	4,514	1.5
Motor vehicles, trailers and semi-trailers	294	0.1
Other transport equipment	6,319	2.1
Furniture, manufacturing n.e.c.	3,327	1.1

Source: Statistics Iceland online information. Available at: http://www.statice.is.

53. The manufacturing sector is export-oriented, given the small size of the domestic market. According to the UNSD Comtrade database exports of manufactured products were some 35% of total merchandise exports in 2004 (including non-ferrous metals); aluminium accounted for 18% of the total (US$509 million), followed by medicaments with 4.3% (US$122 million), and some non-electrical machinery (US$81 million). Aluminium is the second most important merchandise export after fishing products. Exports expanded in value terms by around 14% in 2004, and at an average annual rate of almost 10% over the 2000-04 period.

[44] Agreements have been reached with the Faroe Islands, Greenland/Denmark, Norway, Russia, and the EEC.

[45] For a list of the international agreements and conventions to which Iceland is a party, see Ministry of Fisheries (undated).

54. Imports of manufactured products totalled US$2.7 billion in 2004, representing three quarters of total imports. The largest imports were machinery and transport equipment, which represented about 37% of total imports, particularly automotive products (US$376 million), some non-electrical machinery (US$347 million), office and telecommunications equipment (US$236 million), and other consumer goods.[46] Some 74% of imports of manufactured goods entered Iceland duty free in 2005[47]; the average MFN tariff was 2.5% and the highest rates were applied on imports of clothing and footwear.[48]

55. As reported in Iceland's previous Review, foreign participation in the aluminium and ferro-silicon industries is high, and there has been significant activity in this respect over the review period. Following the merger between Alcan and Swiss-based Alusuisse Lonza AG, in 2000, Iceland's largest aluminium plant, in Straumsvik, is now owned and operated by a subsidiary of the Canadian-based Alcan. The plant was previously owned and operated by a subsidiary of Alusuisse.

56. In March 2003, parliamentary approval was reached for the construction by U.S.-based Alcoa, of an aluminium smelter at Reydarfjordur in eastern Iceland. The smelter is expected to start production in 2007. In tandem, a new hydropower station and a new harbour facility at Mideyri are also being constructed by the National Power Company and the Fjardarbyggd Harbor Fund, respectively.[49] In April 2004, Colombia Ventures Corporation sold the Nordurál primary aluminium reduction facility located in Grundartangi to the U.S.-based Century Aluminium Company. Century Aluminium has invested significantly in expanding the production of this plant in the last two years, from 90,000 tons per year up to 220,000 tons per year.[50]

57. In 2002, the Norwegian based-company Elkem ASA further consolidated its ownership of Icelandic Alloys Ltd., which operates Iceland's only ferro-silicon plant located at Grundartangi, by buying the Government's remaining shares (10.49%), the shares held by the Japanese company Sumitomo Corporation (3.4%), as well as the shares of a number of other shareholders (10.67%). By January 2003, the Elkem Group had achieved 97.2% ownership.[51]

58. A feature of the review period, has been the growth in turnover and export of medicinal and medical products, including, *inter alia*, prosthetic devices, generic products, diagnostic technology, and medical software. Many of the firms involved are specialist small or medium-sized enterprises.[52]

59. The Icelandic authorities stressed that recent international trends and developments have opened up other areas of opportunity for Iceland in international markets. In addition to the above, the authorities indicated that software design and manufacture is a fast growing sector and biotechnology has become a new area of activity. Finally they noted that Icelandic outward investment has steadily increased and thus has provided Icelandic companies with better access to financing and venture capital.

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[46] Imports of goods classified under HS chapter 84 were subject to an average MFN tariff rate of 0.8%; goods under HS chapter 85 faced an average tariff of 4.4%, while imports under HS chapter 87 were subject to an average tariff rate of 1.4%. Imports under these three chapters represented one third of total imports in 2004.

[47] Imports under HS chapters 25, 26, 28, 29, 31, 47, 50, 51, 52, 53, 54, 55, 60, 72, 81, 86, 88, 90 and 92 were entirely duty free.

[48] Imports under chapters 61, 62 and 64 are subject to average tariff rates of 14.2%, 14.4%, and 13.9% respectively.

[49] Alcoa online information. Available at: http://www.alcoa.com/iceland/en/home.asp.

[50] Century Aluminium online information. Available at: http://www.centuryca.com.

[51] Elkem ASA online information. Available at: http://www.elkem.com.

[52] Iceland Export Directory online information. Available at: http://www.icelandexport.is. The main companies include: Össur (http://www.ossur.com); Actavis (http://www.actavis.com); deCODE genetics (http://www.decode.com) and Encode (http://www.encode.is).

(5) ENERGY

(i) Main features

60. Almost all electricity generated in Iceland stems from hydro and geothermal energy. In 2005, a total 8,679 GWh of power was produced, well below Iceland's full potential (estimated at 30 TWh/year for hydro and 20 TWh/year for geothermal energy).[53] Iceland is not an exporter of energy, but a large proportion of domestic electricity generated is used in the production of aluminium and to a lesser extent ferro-silicon, which are exported (see section (4) above). Development of the energy sector is therefore closely linked with investments in these power-intensive industries. Approximately 90% of imported fuel is used for transport and the fishing fleet.[54]

61. The electricity sector remains almost entirely in the ownership of the State or local governments. The National Power Company (Landsvirkjun), jointly owned by the Icelandic State, the City of Reykjavik, and the Town of Akureyri, is dominant in the generation of electricity, and produced 83.4% of Iceland's electricity in 2005. Production by other companies, however, has been gradually increasing. In 2005, a new Act passed in the Parliament removed the tax exemptions previously granted to energy companies. The National Power Company is also the majority owner of IceGrid (Landsnet), which runs the transmission grid and delivers electricity to the whole of the country through several state and regional distributors, of which Reykjavik Energy is the largest.

62. Average tariffs for electricity supplied to energy-intensive industries fluctuated between ISK 1 per kWh and ISK 1.4 per kWh over the period from 1991 to 2002. The retail price of electricity for general consumption is much higher, and fluctuated between ISK 8 per kWh and ISK 13 per kWh (plus VAT) over the same period. Energy subsidies of ISK1.59 per kWh are paid to farmers, and amount to as much as 70,000 kWh per year.[55]

63. A framework programme focused on evaluating and classifying potential sites for electricity production in Iceland has been under way since 1999. Both economic and environmental effects of possible projects are being taken into account. In the first phase of the programme, concluded in 2003, 19 hydropower projects and 24 possible geothermal plant sites were evaluated and consultations carried out.[56] A number of large-scale power stations, in the range of 100 to 700 MW, are now under construction.

64. Close to 90% of houses in Iceland are heated using hot water and steam from geothermal sources. The remaining houses are heated by electricity, generated by hydropower or geothermal steam and to a very small extent, oil and gas. As at early 2006, 22 companies supplied geothermal heating of which Reykjavik Energy was by far the largest. During the review period the number of companies supplying heating has fallen considerably as bigger companies, often supplying both heating and electricity, have bought up smaller district heating systems. The district heating companies are mainly owned by local municipalities; in some cases with some minor state share. The Minister for Industry and Commerce allots exclusive rights to various heating utilities.

65. All major electricity companies are publicly owned, occasionally jointly by the State and some municipalities. The authorities noted that a Ministry of Commerce Action Plan for 2004-07 states that work will be done on the restructuring of electricity companies and state ownership.

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[53] Iceland Export Directory online information. Available at: http://www.icelandexport.is).

[54] National Energy Authority, *Orkumal 2004: Eldsneyti*. Available at: http://www.orkustofnun.is and Statistics Iceland (http://www.statice.is).

[55] National Energy Authority and Ministries of Industry and Commerce (2004).

[56] National Energy Authority and Ministries of Industry and Commerce (2004).

(ii) Institutional and legal framework

66. Iceland maintains restrictions on foreign investment in the energy sector. Under the Act on Investment by Non-residents in Business Enterprises No. 34/1991 (Article 4), only Icelandic-domiciled residents and legal entities may own energy exploitation rights or enterprises involved in producing or distributing energy. These rights were extended to EEA residents and legal entities in 1996 (Act No. 46/1996) and EFTA residents and legal entities in 2002 (Act No. 76/2002). Furthermore agreements may be reached to extend these rights to non-EEA or EFTA residents or legal entities, but these are subject to Parliamentary resolution. There have been no such agreements to date.

67. As a result of its participation in the EEA, Iceland is required to transpose EU legislation; the specific provisions and arrangements on energy as further set out in Annex IV to the agreement. Among these are the EU's Directive on the internal market for electricity. The provisions of Directive 92/96 have been implemented and the Icelandic authorities are in the process of implementing changes due to Directive 54/2003.

68. Since 2003, there have been some important legislative changes in the energy sector designed to promote greater efficiency and competition, driven by Iceland's EEA obligations. The Electricity Act (Act 65/2003 as amended), which came into effect in 2003, paved the way for the separation of electricity transmission and distribution from production and sale. In addition, since 2005 all large electricity consumers (over 100 kW) have been able to choose their supplier. From 1 January 2006, this freedom has been extended to all consumers.

69. Under the 2003 Electricity Act, licences for the construction and operation of electric power plants are granted by the Minister of Industry and Commerce. Previously, parliamentary approval was needed. Power stations of 7 MW or larger are obliged to be connected to the transmission system. Applications may be made to the Minister to construct facilities to allow transit of electricity directly from the power station to the final customer, if the existing transmission system lacks capacity (Articles 5 and 11).

70. As required by the Electricity Act, one company is responsible for electricity transmission in Iceland, and has the exclusive right to build new transmission facilities. This independent transmission system operator, IceGrid (Landsnet hf), was created by Act No. 75/2004. The National Energy Authority (Orkustofnun) sets limits on the maximum income IceGrid is allowed to charge for its services thus indirectly places limitations on the tariffs IceGrid may charge. In addition the law stipulates a maximum allowed profit of the company.

71. A licence must be obtained from the Minister of Industry and Commerce for the construction and operation of distribution systems within specific zones. These licences are exclusive (Article 13). Income, tariffs and profits of the distribution companies are regulated in a similar way to IceGrid. Licences are also required to trade in electricity (Article 18). Seven companies have been authorized to trade in electricity and two applications are pending, as at early 2006.

72. According to the Electricity legislation the National Energy Authority has the function of regulator and administers the general implementation of the Law. More specifically the Authority monitors the licensed transmission and distribution activities; it also monitors the quality and safety of the distribution system. This constitutes an additional role for the Authority, which previously advised the Government on energy issues and natural resources, managed energy research, and worked on long-term energy exploitation plans.

73. The Electricity Act of 2003 did not affect an existing owner’s exclusive rights to operate a heating distribution, although companies also engaging in the supply of electricity are required to keep separate accounts for the different functions. The Ministry is currently preparing a proposal for a new Act on district heating systems, which will set requirements concerning their activities and revise the system of exclusive supplying rights.[57]

74. A National Energy fund provides loans to small geothermal heating companies with the objective of developing renewable energy sources. While the interest rate is market based, the loan is guaranteed in the event of failure of the projects undertaken. According to the authorities the level of state support is around US$0.5 million per year.

(6) SERVICES

(i) Main features

75. The services sector has continued to expand since Iceland's previous Review, to around 80% of GDP in 2004. This expansion has been driven largely by financial services, and real estate, renting, and business activities. The financial services sector's contribution to GDP measured 7.3% in 2004, up from 5.7% in 1999; the contribution of real estate, renting, and business activities increased from 12.9% to 14.6% over the same period. Trade in commercial services has also expanded rapidly. Service exports increased by an average of almost 11% per year between 1998 and 2004, and service imports by around 12%.

76. Under the GATS, Iceland undertook sector-specific commitments in business services, telecommunications services, construction and related engineering services, distribution services, financial services, tourism and travel related services, as well as on environmental, recreational, cultural and sporting, and transport services (Table AIV.1). Iceland bound market access and national treatment without limitations on cross-border supply, consumption abroad, and commercial presence for a number of service activities, including: telecommunication services, construction and related engineering services, distribution services and transport services. Market access was left unbound with respect to the presence of natural persons, except for the temporary entry of executives, managers, specialists, and service sellers.

77. Some limitations on market access and national treatment specified in Iceland's GATS Schedule are applied to all scheduled sectors as specified in the horizontal commitments in Iceland's Schedule. These cover services provided in Iceland through commercial presence or presence of natural persons, and are generally in the form of reporting requirements and investment limitations.

78. Other limitations to national treatment exist: national treatment is accorded to subsidiaries of non-EEA companies formed in accordance with the law of, and established in, an EEA State, but not to branches or agencies. Eligibility for subsidies may be limited to juridical persons established within the territory of Iceland. Regarding the presence of natural persons, subsidies available to natural persons may be limited to Icelandic citizens. Subsidies related to research and development are unbound.

79. Iceland's final list of GATS Article II MFN exemptions cover audio-visual and air transport services. They include also some measures to maintain and develop Nordic cooperation. All these measures are intended by the authorities to have an indefinite duration.

[57] National Energy Authority, *Orkumal 2004: Jardhiti*. Available at: http://www.orkustofnun.is/Apps/WebObjects/Orkustofnun.woa/swdocument/4004/1.+%C3%A1rg.+3.+tbl.+jar%C3%B0hiti.pdf.

(ii) Telecommunications

(a) Main features and developments

80. The Icelandic telecommunications sector has undergone major change since 1998 with the separation of postal and telephone services, the creation of Iceland Telecom Ltd. (also known as Síminn) and the opening up of the sector to competition. Over the review period there have been a number of legislative developments, the emergence of new players in the Icelandic telecommunications sector, merger and acquisition activity, as well as the privatization of Iceland Telecom. Reforms were predominantly driven by EEA membership requirements. Liberalization and regulatory commitments undertaken have also been bound in the WTO as a result of Iceland's participation in the post-Uruguay Round negotiations on basic telecommunications.

81. One of the major developments over the review period was the privatization of Iceland Telecom. In May 2001, legislation was passed providing for the privatization of Iceland Telecom, however, the share offering was unsuccessful, mainly due to prevailing uncertainty in global financial markets and the telecommunications sector in general.[58] However, on 5 August 2005 Iceland Telecom was sold for ISK 67 billion to a consortium of predominantly Icelandic investors under the name Skipti Ltd.[59] In addition, since 1998, there have been new entrants into, and consolidation within, the telecommunications market.

82. As at end 2005, the telecommunications market in Iceland was a de facto duopoly with both Iceland Telecom and Og Vodafone providing basic telecommunications services. Both telecom providers are classified as having "significant market power" in certain service markets and hence may be subject to various obligations, imposed by the Post and Telecom Administration (PTA) with respect to access to infrastructure, interconnection and carrier selection and pre-selection.[60] Under Article 18 of the Electronic Communications Act, an undertaking with significant market power is deemed to have, either individually or jointly with others "a position of economic strength in a certain market which enables it to prevent effective competition and to operate to a substantial extent without concern for competitors, customers and consumers." The assignment of market power is now based on competition law principles, rather than a 25% market share as in the previous Act.[61] Both Iceland Telecom and Og Vodafone have been making investments in related areas, for example, both bought television stations in 2004. There have also been some infrastructural developments over the review period with respect to telecommunications, notably the entry into operation of a new submarine transmission cable (FARICE) linking Iceland to Scotland via the Faeroe Islands. EFTA opened an information investigation procedure regarding state aid to the FARICE submarine project in 2005.

83. As documented by the OECD[62], the telecommunications sector in Iceland has witnessed expansion in a number of areas in recent years, among them: telecom revenue increased from US$89 million in 1991 to US$319 million in 2003, and the share of telecom revenue as a percentage of GDP over-doubled during the same period; there was a major increase in subscriptions to cellular phones, from 17,409 in 1993 to 279,670 in 2003 (equalling 96.7 subscribers per 100 inhabitants); the number of secure servers (one indication of e-commerce access and supply) increased from 13 in 1998 to 249 in 2004. In addition, the OECD reports that of all OECD countries

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[58] Prime Minister's Office, Press Release of 3 January 2002. Available at: http://eng.forsaetisraduneyti.is/ministry/privatisation/nr/1002

[59] PTA Press Release of 7 September 2005. Available at: http://www.pta.is/default.asp?cat-id=188 module_id=220&element_id=721.

[60] Electronic Communications Act No. 81/2003, Articles 27 to 34, Article 53.

[61] PTA (2003).

[62] OECD (2005) Communications Outlook.

Iceland has the least expensive domestic residential telecommunication services, and has been taking the lead in the development of DSL access. As reported by the PTA, by the end of 2004, around half of Icelandic homes had an ADSL high speed internet connection.[63]

(b) Institutional and legal framework

84. The Minister of Communications is responsible for policy formulation in the telecoms sector. One of the stated priorities of the Icelandic Government is to develop the information society in Iceland so as to be at the forefront of the world's nations in terms of "the utilization of information technology in the service of improved human existence and prosperity", and within the context of this larger picture, the objectives for the telecoms sector is for information and telecommunications technologies to be "mobilized to improve the competitiveness of the Icelandic economy, increase productivity and proliferate the possibilities of exporting Icelandic inventiveness.[64]

85. Electronic communications in Iceland are administered on a daily basis by the Post and Telecom Administration, which was created in 1997. The PTA's seven key areas of responsibility with respect to electronic communications are: implementing the Electronic Communications Act and supervising electronic communications as provided for in the Act; encouraging competition in postal and electronic communications services and preventing unfair business practices; participating in developing the market for electronic communications and information technology; safeguarding the public interest; advising the authorities and ministries and ensuring that Iceland fulfils its international obligations as well as making recommendations, if necessary, for amendments to acts and regulations; participating in cooperation resulting from international obligations; and other activities.[65] The main rules and regulations currently in force in the area of telecommunications are outlined in Table IV.5.

86. Telecommunications legislation has been revised on a number of occasions since the mid-1990s. The 1996 Telecommunications Act opened up the sector to international competition in 1998; until then, only the state monopoly was allowed to offer telecommunications services in Iceland. A new Telecommunications Act entered into effect in January 2000; and Regulation No. 734/2000, confirmed the right of companies in the telecoms sector in WTO Member countries to offer their services in Iceland.

87. Most recently, the Electronic Communications Act No. 81/2003 took effect in July 2003; it is intended to implement required EEA legislation.[66] As a result of this legislation, natural persons and legal entities established within the EEA and within WTO Member states have a general authorization, and therefore do not need a licence, to start operation, unless specific frequencies are involved.[67] Undertakings, however, must notify the PTA, which keeps a register. An individual licence is required for all frequencies except open spectrum (2400-2483.5, 5150-5350, 5470-5725 and 5725-5875 MHz). In most cases the procedure is simple and frequencies are assigned by the PTA within six weeks from receipt of application. In frequency ranges where demand is likely to exceed

[63] PTA (2004).

[64] Document issued by the Icelandic Government entitled "The Icelandic Government's Vision of the Information Society" (http://eng.forsaetisraduneyti.is/information-society/nr/890#3). Subsequent official documents issued in related areas include; "Resources to Serve Everyone: Policy of the Government of Iceland on the Information Society 2004-2007" and the "Telecom Policy Statement 2005-2010, Report by the Steering Group appointed by the Minister of Transport and Communications".

[65] Act on the Post and Telecom Administration, No. 69/2003 (Article 3).

[66] EEA legislation includes: Annex XI, Regulation 2887/2000/EC, Directives 1999/5/EC, 2002/19/EC, 2002/20/EC, 2002/21/EC, 2002/22/EC, 2002/58/EC and 2002/77/EC.

[67] Electronic Communications Act No. 81/2003, Chapter III and Regulation 86/2002.

supply, the PTA may decide to limit the number of rights of use. In such cases frequencies have most often been assigned following a "beauty contest". The method for assignment of specific frequencies must be published and applications invited by advertisement (Article 9).

Table IV.5
Telecommunications legislation currently in force

Laws
Act on the Post and Telecom Administration No. 69/2003
Electronic Communications Act No. 81/2003
Rules and regulations
Regulation on secrecy and protection of telecommunications, No. 83/1986
Regulation on frequency bands for wireless telecommunication services, No. 373/1994
Regulation on the approval of subscriber equipment, No. 598/1994 (amended)
Regulation about standardization in the fields of information technology and telecommunications, No. 35/1995
Regulation on access to leased lines, No. 608/1996
Regulation regarding premium rate services, No. 359/1997
Regulation about the Appellate Committee for Electronic Communications and Postal Affairs, No. 378/1999
Regulation concerning the telecommunication equipment and telecommunications to and from Icelandic ships, No. 53/2000
Regulation regarding universal service, No. 641/2000 as amended
Regulation on the right of WTO Member companies to offer their services in Iceland, No. 734/2000
Regulation on separation of electronic communications networks and cable television networks, No. 866/2000
Rules for number portability, No. 401/2001
Regulation on the use of standards for television signals, No. 532/2001
Rules for carrier selection and carrier pre-selection in telephone networks, No. 280/2002
Rules for the planning of numbers and the use of numbers, number series and addresses, No. 318/2003
Rules about general authorisation to operate electronic communications networks or services No. 345/2005

Source: Post and Telecom Administration online information. Available at: http://www.pta.is.

88. The Act also contains provisions on transparency and non-discrimination; rules on number portability[68], and on carrier selection and pre-selection[69]; and provisions relating to competition within the sector.[70] The right to interconnection is established in Chapter VII of the Act, and the PTA is charged with endeavouring to "ensure access and interconnection and interoperability of services in a satisfactory and efficient manner" (Article 25) and may, *inter alia*, impose obligations with respect to open and non-discriminatory access and price control. According to the authorities, in early 2006 the PTA was undertaking a market analysis of the 18 telecoms sub-markets and is likely to issue new obligations regarding access and interconnection either in 2006 or 2007.

89. The Electronic Communications Act provides for all users to be entitled to universal service at the same tariff rate throughout the country. The universal service obligation relates to basic telephony, data (128 Kb connection), and some other services. To ensure this obligation is met, the PTA may place obligations on electronic communications providers and set minimum quality requirements. According to the authorities, minimum quality requirements have been issued by the PTA. The PTA also holds custody of an equalization fund to support universal service operations that are either unprofitable or run at a loss. The fund is financed by a 0.12% fee levied on the turnover of all electronic communications providers. The authorities note that the turnover of the fund has been

[68] Electronic Communications Act No. 81/2003, Article 52 and regulations: 401/2001, cf. reg. 840/2001, 508/2003 and 83/2004.

[69] Electronic Communications Act No. 81/2003, Article 53 and Regulation 280/2002.

[70] Competition-related provisions in the Electronic Communications Act No. 81/2003 include: rules on mergers with respect to rights to use frequencies (Article 8); provisions relating to markets (Articles 16 to 18) as well as to interconnection of networks and services and access to them (Chapter IV).

small, and has just provided for the answering of emergency calls. They also indicate that government funding will be targeted at expanding GSM and broadband networks into non-commercially viable areas; ISK 2.5 billion is to be allocated to this project until 2009.

90. Public electronic communications network equipment (both domestically produced and imports) must meet certain technical requirements and bear the CE mark as confirmation (Chapter III(2)(viii). Equipment that is operated without authorization may be confiscated.

91. Violations of the provisions of both the Electronic Communications Act and the Act on the Post and Telecom Administration must be rectified within a month of their notification by the PTA. If violations are not rectified, the PTA has authority to subject providers to daily fines, and to cancel the right to use numbers or the general authorization to operate. Serious or repeated violations may result in imprisonment. Rulings by the PTA may be referred to the Rulings Committee for electronic communications and postal affairs.[71] The PTA has a responsibility to promote competition applying sector-specific regulation. General competition rules are also applicable to the electronic communications markets. The Competition Authority is responsible for the enforcement of general competition rules; an agreement has been reached between the PTA and the Competition Authority in this regard.

92. Iceland's commitments in the extended WTO Negotiations on Basic Telecommunications Services supplement the commitments contained in its initial GATS Schedule.[72] The Icelandic Schedule covers basic and value-added services, for which Iceland has agreed to impose no limitations on market access or national treatment for cross-border supply, consumption abroad, and commercial presence. Market access through the presence of natural persons was left unbound except as indicated in the horizontal commitments. The Schedule incorporates, under additional commitments, the telecommunications Reference Paper negotiated in the context of the extended negotiations.

93. In the context of the Doha Development Agenda, Iceland has submitted an initial and a revised offer.[73] In its revised conditional offer, Iceland proposes removing a limitation on investment specified in the horizontal commitments of its Schedule, which specifies that total investment by a non-resident or the joint investment by financially related non-residents in enterprises in communications services may not exceed ISK 250 million (US$4 million) within a year unless a special concession is given. This would be replaced by an obligation on the part of service providers to inform the Ministry of Commerce of investments by non-residents in business enterprises in Iceland, and the Central Bank of Iceland of investments by non-residents in securities in Iceland.

(iii) Financial services

(a) Introduction

94. Iceland's GATS market access and national treatment commitments cover the full spectrum of financial services.[74] These commitments are undertaken in accordance with the Understanding on Commitments on Financial Services.

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[71] Post and Telecom Administration Act No. 69/2003, Article 13.

[72] WTO document GATS/SC/41, 15 April 1994 and WTO document GATS/SC/41/Suppl.1, 11 April 1997.

[73] WTO document TN/S/O/ISL/Corr.1, 17 July 2003 and WTO document TN/S/O/ISL/Rev.1, 14 June 2005.

[74] WTO document GATS/SC/41/Suppl.2, 26 February 1998.

95. Financial legislation has undergone a process of extensive review, restructuring, and update since Iceland's 2000 Trade Policy Review. This process culminated in the adoption of the Act on Financial Undertakings, in force since January 2003.[75] The Act governs the activities of banks and other credit institutions, electronic money undertakings, securities firms and brokerages, and management companies for mutual and investment funds (also known as UCITS). The main legislation in the insurance sector is the Act on Insurance Activities.[76]

96. The Ministry of Commerce defines financial sector policy. The Central Bank is tasked with promoting the efficiency and safety of the financial system.[77] It monitors bank liquidity and foreign exchange balances, and conducts the systemic oversight of the payment and settlement systems.[78] The Financial Supervisory Authority (Fjármálaeftirlitið or FME) is responsible for the supervision of financial and insurance companies and pension funds.[79] Financial sector regulations may be issued by the Ministry of Commerce; additional rules and guidelines may be issued by FME and the Central Bank (only with respect to bank liquidity and foreign exchange balances, and payment and settlement systems).[80]

(b) Banking services

97. There are four commercial banks and 24 savings banks operating in Iceland. The three major banks (all commercial banks) account for approximately 90% of total bank assets.[81] The current structure of the banking sector is the result of privatization and intense consolidation between 1998 and 2003.[82] Two of the commercial banks were publicly owned until 2003. There is one foreign bank branch operating in Iceland, but no foreign bank subsidiaries or representative offices.

98. The spread between lending and borrowing rates declined from 3.7% in 1997 to 2.3% in 2004, partly reflecting increased levels of competition.[83] According to the OECD, competition in the investment banking segment appears to be "fierce".[84] In contrast, competition in lending to small and medium-sized enterprises seems to be less vigorous.[85]

99. There is also a state-owned Housing Financing Fund (HFF), created in 1999. HFF is the largest institution in the financial system. Its purpose is to promote home ownership by providing affordable mortgage credit. Until mid 2004, HFF accounted for about 80% of the residential mortgage market; however, its share has fallen to about 65% (December 2004) with the recent entry of commercial banks into this market. In April 2004, the Bankers' and Securities Dealers' Association of Iceland lodged a complaint with the EFTA Surveillance Authority, alleging that "the current legislation in Iceland on the operation of the State Housing Financing Fund is incompatible with the EEA Agreement, in particular the competition rules, the rules on state aid, free movement of services, capital and the freedom of establishment of the EEA Agreement".[86] The Authority

[75] Act No. 161/2002, 13 December 2002.
[76] Act No. 60/1994, 11 May 1994.
[77] Act No. 36/2001 on the Central Bank of Iceland.
[78] Central Bank of Iceland online information, "Financial stability and Central Bank tasks". Available at: http://www.sedlabanki.is/lisalib/getfile.aspx?itemid=2918 [19 December 2005].
[79] Article 3, Act No. 87/1998 on Official Supervision of Financial Operations, 16 June 1998.
[80] Agreement between the Financial Supervisory Authority and Central Bank of Iceland on Payment and Settlement Systems, 28 March 2003.
[81] FME (2004a).
[82] For details on the process of consolidation, see Central Bank of Iceland (2005a).
[83] Measured in relation to bank total assets.
[84] OECD (2005a).
[85] OECD (2005a).
[86] EFTA Surveillance Authority Decision No. 213/04/COL, 11 August 2004.

concluded that, although the HFF system involved state aid, this aid was compatible with the EEA Agreement.[87] In November 2004, the Bankers' and Securities Dealers' Association of Iceland appealed this decision. The case is pending before the EFTA Court (January 2006).[88]

100. Several Icelandic banks have made significant international acquisitions recently, particularly in other Nordic countries and the United Kingdom.[89] Partly as a result, total bank assets almost doubled between 2003 and 2004, to reach 360% of GDP. Half of the assets of the three major banks are held by their foreign subsidiaries.[90]

101. Foreign banks may establish a subsidiary in Iceland. All banks, including foreign-owned subsidiaries, must be organized as limited liability companies.[91] In principle, banks are permitted to provide securities services, but not insurance, unless they set up a separate company for that purpose.[92]

102. All banks, including foreign-owned subsidiaries, are required to obtain a licence to operate in Iceland. FME is responsible for issuing licences. The following information must accompany a bank's licence application: proposed activities; articles of association; operational structure and internal organization; business plan and budget; founders, shareholders, management officers, and board of directors; confirmation by an accountant that the share capital has been paid; "close links" to other entities; and any other relevant information required by FME.[93] FME must notify the applicant of its decision "as promptly as possible".[94] The statutory time limit available to FME is three months; in practice, applications are processed in one-and-a-half months. FME must explain the grounds for a negative decision.[95] FME has not issued any negative decisions since 2003, when it took over responsibility for issuing banking licences from the Ministry of Commerce.

103. The minimum capital requirement to establish a commercial or savings bank in Iceland is ISK 450 million (approximately €6 million in December 2005) or €5 million, if the euro equivalent of ISK 450 million is less than €5 million.[96] This requirement applies to all banks licensed to operate in Iceland, regardless of ownership. A grandfather clause allows savings banks in operation prior to 2003 to maintain their capital at their 1993 level.[97]

104. The founders of a bank in Iceland must reside in Iceland, unless they are EFTA or EEA citizens.[98] The founders can be natural or legal persons. Bank managers and at least half of the board members must be EFTA, EEA, or OECD citizens and residents.[99] The Ministry of Commerce can

[87] EFTA Surveillance Authority Decision No. 213/04/COL, 11 August 2004.

[88] EFTA Court, Action brought on 23 November 2004 by the Bankers' and Securities Dealers' Association of Iceland against the EFTA Surveillance Authority (Case E-9/04). Available at: http://www.eftacourt.lu/default.asp?layout=article&id=239 [2 January 2006].

[89] See Neville (2005).

[90] See Neville (2005).

[91] Article 13, Act No. 161/2002.

[92] Articles 20 and 23, Act No. 161/2002.

[93] Article 5, Act No. 161/2002; the provisions on close links are contained in Article 18.

[94] Article 6, Act No. 161/2002.

[95] Article 7, Act No. 161/2002.

[96] Article 14, Act No. 161/2002.

[97] Article 77, Act No. 161/2002.

[98] Article 11, Act No. 161/2002.

[99] Article 66, Act Respecting Public Limited Companies, No. 2/1995; Article 42, Act Respecting Private Limited Companies, No. 138/1994; and Announcement Respecting General Exemption from Conditions of Residence of the Limited Company Legislation, No. 260, 16 April 1997.

waive these nationality and residency requirements for other citizens.[100] In the context of this Review, the Icelandic authorities indicated that they have not received any waiver requests (as at February 2006), and that any future requests would be assessed on a case-by-case basis.

105. There are no limitations on foreign ownership of banks in Iceland. Foreign and domestic investment that is aimed at acquiring 10% or more of the capital or voting rights of a bank, or which enables the exercise of a "significant influence" over the bank's management, is subject to FME approval.[101] FME approval is also required when a foreign or domestic investor's participation in a bank exceeds the thresholds of 20%, 33%, or 50%.

106. Banks in Iceland are allowed to hold equity in financial and non-financial firms. Equity held in firms that pursue "ancillary" activities is not subject to limitations.[102] In contrast, a bank's qualifying holding in a non-financial firm may not exceed 15% of the bank's funds, as defined in the Act on Financial Undertakings.[103] A bank's total qualifying holdings in non-financial firms may not exceed 60% of the bank's funds.

107. Foreign banks may set up a branch in Iceland.[104] In this regard, banks established and licensed in the EEA benefit from an automatic approval process. A branch may begin operations two months after receipt by FME of a notification of the branch's proposed activity from the home-country supervisor. The home-country supervisor must also confirm that it will provide "satisfactory supervision" of the bank's activities, and that the bank fulfils FME's "sound and prudent" management requirements and other conditions listed in Regulation No. 244/2004.[105] There are no published criteria for assessing "sound and prudent" management requirements. A branch may only pursue activities for which its parent is licensed in the home country. Banks established and licensed in Switzerland benefit from the automatic approval process to set up branches (or to provide cross-border services) provided that "the same requirements are made of them as of financial undertakings established in states of the EEA and a cooperation agreement has been concluded between [FME] and the competent Swiss authorities".[106] No such agreement has been concluded (February 2006).

108. Banks established and licensed outside the EEA are required to obtain FME authorization to open a branch. To this end, the bank's home-country licence must cover the same activity that the bank proposes to carry out in Iceland; the bank must also be subject to "comparable supervision" in its home country.[107] The regulations related to this provision are being updated (February 2006).[108]

109. Branches of EEA banks are not subject to stand-alone requirements on capital adequacy or loan limits. Their activities are subject to consolidated supervision with the parent bank by the home country supervisor. Stand-alone prudential requirements applied to branches of non-EEA banks. These are being updated.[109]

[100] Article 11, Act No. 161/2002.
[101] Article 40, Act No. 161/2002.
[102] Article 21, Act No. 161/2002.
[103] Article 28, Act No. 161/2002.
[104] Chapter V, Act No. 161/2002.
[105] Article 2.
[106] Article 31, Act No. 161/2002.
[107] Article 33, Act No. 161/2002.
[108] The regulations under review are contained in Regulation of a Branch and a Representative Office of a Credit Institution Established in a Country Outside the European Economic Area, No. 307/1994, 25 May 1994.
[109] Regulation No. 307/1994.

110. Foreign banks may also provide cross-border services in Iceland.[110] To do so, banks established and licensed in the EEA must complete an automatic approval process similar to the process for setting up a branch. Banks may begin offering cross-border services immediately after FME receives the relevant notification from the home-country supervisor. EEA banks may only provide cross-border services for which they are licensed in their home country.

111. Banks established and licensed outside the EEA must obtain FME authorization to provide cross-border services. In this regard, the bank's home-country licence must cover the same activity that the bank proposes to carry out in Iceland; the bank must also be subject to "comparable supervision" in its home country.[111] FME has approved 117 credit institutions to provide cross-border services; all are licensed in the EEA.

(c) Insurance services

112. Iceland's insurance industry comprises four life insurance companies and eight non-life companies, including one that is wholly state-owned and another that is foreign-owned (February 2006).[112] In addition, there are two branches of an EEA insurance company, one offering life insurance and the other non-life insurance. About 230 EEA companies are registered as offering cross-border insurance services.[113] Total assets of life insurance companies are ISK 8.82 billion, around 1% of GDP.[114] Total assets of non-life insurance companies are almost 11 times that amount.

113. The non-life insurance market has been dominated by three companies, whose combined market share in total written premiums was around 94% in 2002. The Competition Authority recently concluded a seven-year cartel investigation, which found that the three largest companies had engaged in practices harmful to competition.[115] According to the Icelandic authorities, this investigation led to changes in the companies' practices, and in the activities of the Association of Icelandic Insurance Companies.

114. Foreign insurance companies may establish a subsidiary in Iceland. All insurance companies, including foreign-owned subsidiaries, are required to be organized as limited liability companies or mutual companies. Life and non-life insurance services cannot be provided through the same company; however, life insurance companies may provide sickness and accident insurance.

115. Insurance companies, including foreign-owned subsidiaries, must obtain a licence to operate in Iceland. Licences are granted for specific life and non-life categories of insurance by the Minister of Commerce after consulting with FME.[116] Licence applications must contain the following information about the insurance company: legal form of establishment; articles of association and minutes of the initial shareholders' meeting; founders; share capital; "close" connections with other companies; proposed activities; business plan; confirmation that minimum solvency margin provisions have been fulfilled; basis for calculating premiums and other variables; rules on information requirements from policyholders; and conditions governing compulsory insurance.[117] FME must issue an opinion within six months of receiving an application. When rejecting an

[110] Chapter V, Act No. 161/2002.
[111] Article 33, Act No. 161/2002.
[112] FME (2004b).
[113] FME online information. Available at: http://www.fme.is/fme-eng.nsf/pages/ForInsurComp.html [15 November 2005].
[114] FME (2004b).
[115] OECD (2005a).
[116] The categories for which licences are issued are listed in Articles 22 and 23, Act No. 60/1994.
[117] Article 21, Act No. 60/1994.

application, FME must provide the reasons underlying its decision in writing. FME maintains a public register of all licensed insurance companies in Iceland.

116. The minimum solvency margin varies according to the type of service provided. It is ISK 255 million (or €3 million, whichever is the higher, except for non-life insurance companies engaged in liability insurance, which are subject to a minimum solvency margin or ISK 170 million (or €2 million, whichever is the higher.

117. A majority of the founders of an insurance company in Iceland are required to reside in Iceland.[118] The founders can be natural or legal persons. EFTA and EEA citizens residing in an EFTA or EEA country are not required to comply with this requirement. Managers and the board members of insurance companies organized as limited liability companies must reside in an EFTA or EEA country.[119] The Minister of Commerce can waive these nationality and residency requirements for non-EFTA or non-EEA citizens. In the context of this Review, the Icelandic authorities indicated that they have not received any waiver requests (February 2006), and that any future waiver requests would be assessed on a case-by-case basis.

118. There are no limitations on foreign ownership of insurance companies in Iceland. Foreign and domestic investment that aimed at acquiring 10% or more of the capital or voting rights of an insurance company, or that enables the exercise of a "significant influence" over the company's management, is subject to notification and approval by FME.[120] FME notification and approval is also required when an investor's participation exceeds the thresholds of 20%, 33%, or 50%. FME may refuse acquisitions of or increases in shares or voting rights if the investor is not qualified to ensure "the sound and prudent operation of the company". In such cases, FME must provide the investor with the reasons that underlie its decision. FME has never blocked an acquisition (February 2006).

119. Insurance companies licensed in the EEA and with head offices there may open a branch in Iceland. The approval process is automatic and involves the submission of specific information to FME, including a certificate from the home-country supervisor that the company meets the home-country minimum solvency margin.[121] A branch may start operations immediately after FME has notified the company that the information provided is complete. FME must issue its notification within two months of receiving the application. A branch can only provide services for which its parent is licensed in the home country. The company is required to designate a representative in Iceland.

120. Foreign insurance companies licensed outside the EEA and with head offices outside the EEA may not set up branches in Iceland unless their home countries grant reciprocal treatment to Icelandic companies.[122] Insurance companies that fulfil the reciprocity requirement must apply for a licence to open a branch. Their application is subject to the same requirements as for subsidiaries. In addition, FME must "consult" all other EEA countries before issuing the licence.[123] The company must designate a representative in Iceland.

121. Branches of non-EEA insurance companies are required to fulfil stand-alone minimum solvency margins. The solvency margin cannot be less than one-half of the amount applicable to

[118] Article 14, Act No. 60/1994.
[119] Article 66, Act No. 2/1995; Article 42, Act No. 138/1994; and Announcement No. 260.
[120] Article 39, Act No. 60/1994.
[121] The information required by FME is listed in Articles 64 and 65, Act No. 60/1994.
[122] Article 71, Act No. 60/1994.
[123] Article 71, Act No. 60/1994.

insurance companies licensed in Iceland.[124] Branches assets in Iceland must amount to the higher of one half of the minimum solvency margin for insurance companies or one-third of their individual minimum solvency margin. The solvency requirement may be waived when the overall solvency margin of a company's branch in Iceland and other branches in EEA countries is subject to consolidated supervision in one EEA country. A regulation has been issued to implement this provision.[125] Branches must place as a guarantee fund one-fourth of their minimum solvency margin in a location approved by FME.[126]

122. The provision of cross-border insurance services is limited to insurance companies licensed in the EEA and with head offices there.[127] In this regard, EEA companies benefit from an automatic approval process similar to that for opening a branch.[128] Companies providing cross-border services in third-party motor liability insurance must designate a representative in Iceland.

123. Insurance brokers must obtain a licence from and register with FME.[129] Licences issued in other EEA countries are deemed equivalent to Icelandic licences.[130]

(iv) Air transport

(a) Main features

124. The air transport industry plays a significant role in Iceland's economy. The turnover of airline operations in Iceland amounted to 5% of GDP in 2004, which is much higher than in many other European nations.[131]

125. There are five international airports in Iceland, and eight additional airports provide scheduled flights. More than 95% of international traffic goes through Keflavík airport, near Reykjavík. The Foreign Ministry has jurisdiction over the running of Keflavík airport[132], which is a joint civil and military airport operated by the Civil Aviation Authority (CAA) and the U.S. Navy.[133] All main airports are government-owned and run.

126. The number of passengers flying to and from Iceland through Keflavík airport increased from around 280,000 in 1993 to over 1,360,000 in 2004. Similarly, air transport of freight through Keflavík airport tripled over the same period. In the period 1993 to 2003, freight volume from Iceland rose from 8,135 tonnes to 24,964 tonnes, and freight to Iceland rose from 5,452 tonnes to 15,590 tonnes.[134]

127. Competition on international routes to and from Iceland has increased in the review period with the arrival of a new low-cost airline Iceland Express, in 2003. The other airline offering international flights is Icelandair, in 2006, Scandinavian Airlines and British Airways will start

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[124] Article 72, Act No. 60/1994.

[125] Regulation No. 555/1997 on Co-operation with Other European Economic Area Countries on Supervision with Solvency of Branches of Insurance Companies with Headquarters Outside the European Economic Area.

[126] Article 72, Act No. 60/1994.

[127] Article 65, Act No. 60/1994.

[128] Article 65, Act No. 60/1994.

[129] Article 80, Act No. 60/1994.

[130] Article 3, Regulation No. 853/1999.

[131] Economics Institute (2004).

[132] Law 106/1954 on the Supervision of Defence Areas.

[133] Keflavik Airport online information. Available at: www.keflavikairport.com/history.html.

[134] Statistics Iceland online information. Available at: www.statice.is.

regular flights to Iceland. A total of 11 airlines are in operation in Iceland including those providing rental and cargo services. Air transport in the domestic market is dominated by Landsflug and Flugfélag Íslands. Air Atlanta Icelandic is one of the world's largest aircraft, crew, maintenance, and insurance (ACMI) service providers. It has 50 aircraft and operates cargo and passenger transport services. Since its creation in 1986, it has concluded wet leasing agreements, *inter alia*, with Caribbean Airways, Air Afrique, Finnair Cargo, Lufthansa, Sudan Airways, and Arabian Airlines.[135]

128. The Competition Authority is responsible for ensuring that pricing policy and other arrangements do not breach competition law. In 2003, the Competition Authority ruled that Icelandair had breached competition laws and misused its dominant market position in a price war over the two routes then offered by Iceland Express.[136] In 2005, the FL Group signed an agreement to purchase Iceland's Bluebird Cargo Company and its associated freight forwarder for ISK 3.8 billion (US$60 million) and to assume ISK 1.4 billion (US$22 million) in aircraft debt obligations.[137] The two organizations joined Icelandair Cargo a subsidiary of the Icelandair Group that operates cargo services. In June 2005, the Competition Authority ruled that the merger could take place only under certain conditions to ensure competition in the air cargo industry to and from Iceland.

129. Iceland's civil aviation industry is subject to EEA competition laws. In 2003, one case was referred to the EFTA Court regarding Iceland's air passenger tax, which was higher for flights from Iceland to other EEA destinations than for domestic flights or flights to Greenland and the Faroe Islands.[138] The EFTA Court ruled that the discriminatory application of the tax restricted the freedom to provide services within the EEA.

130. According to the Icelandic authorities, procedures and fees are the same for both domestic and international airline companies. The Government, however, provides support for air transport to a number of domestic destinations that have not proven economically viable. ISK 90 million was granted in 2001; grants are given to airlines via an open competition.[139] According to the Ministry of Transport, ISK 140 million per year will be set aside to support domestic flights until 2009.

131. In its GATS Schedule of Commitments, Iceland listed market access and national treatment with no limitations for consumption abroad and commercial presence in maintenance and repair of aircraft and parts. The authorities indicate that, in practice, most of these services are provided by Icelandic companies. For sales and marketing and for computer reservation systems (CRS), market access was listed with no limitations in cross-border supply, consumption abroad or commercial presence. National treatment for cross-border supply and commercial presence remains unbound for sales and marketing of air transport through CRS provided by a CRS parent carrier. The presence of natural persons was left unbound except as provided in the horizontal commitments. Iceland's list of MFN exemptions covers CRS and sales and marketing of air transport services. The exemptions reserve the possibility for Iceland to apply the country-reciprocity principle in the case of CRS system vendors or of parent and participating air carriers. In its revised offer submitted in the context of the

[135] Air Atlanta Icelandic online information. Available at: http://www.atlanta.is.

[136] The Competition Authority online information. Available at: http://www.samkeppni.is/frettatilkynningar/index.htm.

[137] The FL Group is an investment company with an emphasis on investments in the flight and tourism industries. Icelandair, Icelandair Cargo, Loftleioir Icelandic, Air Iceland Bluebird Cargo and former Danish carrier Sterling are all subsidiaries of the group.

[138] Case E-1/03, EFTA Surveillance Authority v. The Republic of Iceland, 12 December 2003.

[139] Ministry of Communications (2003), Transport, Transport Policy Plan 2003-2014. Available at: http://samgonguraduneyti.is/media /Skyrsla/Samgonguaaetlun2003_2014.pdf.

Doha Development Agenda negotiations, Iceland proposes to remove these national treatment limitations.[140]

(b) Institutional and legislative developments

132. Air transport in Iceland is regulated by the Ministry of Communication. The CAA reports to the Ministry.[141] The Civil Aviation Board provides advice to the Ministry and the Director General of the CAA.[142] The Aircraft Accident Investigation Board reports directly to the Minister. Both the Civil Aviation Board and the Aircraft Accident Investigation Board are independent bodies.

133. The role of the CAA is three-fold. Firstly, it has a monitoring role focused on maintaining flight safety and security; this involves monitoring the airworthiness of aircraft, management of air carrier operators, and issuing licences for pilots and others working in the industry. Secondly, it provides services to the industry in the form of running of airports and air traffic control, as well as providing information for pilots and others in the industry. Thirdly, the CCA carries out various administrative functions and takes part in international cooperation on behalf of Iceland. In 2005, a steering committee on the future of air transport in Iceland, appointed by the Ministry of Transport, suggested separating air traffic and transport services from administration and security monitoring, which are currently all covered by the CAA, and establishing a state-owned public limited company to run the service aspects of the air transport sector. A decision to carry out these changes was taken by the Minister of Transport in August 2005. Draft legislation was sent for comments in late December 2005 to be introduced to the Parliament in late January or February 2006. The change is planned to take place on 1 January 2007.

134. The main legislation regulating the industry is the Aviation Act of 1998 (Table IV.6). There has been a good deal of legislative activity over the review period, including implementation of EEA obligations; however, only minor changes have been made to the Aviation Act.

Table IV.6
Main air transport-related legislation

Act on Aviation, No. 60/1998 (with amendments)
Act on Investigation of Aircraft Accidents, No. 35/2004
Regulation on freight transportation, No. 51/1976, with amendments
Regulation on transportation of people, No. 53/1976 with amendments
Regulation on rules of the air, No. 55/1992 with subsequent amendments
Notice on air operator's licence, No. 439/1994 (Implementation of EC Regulation 2407/92)
Regulation on the mutual acceptance of personnel licences within the EEA, No. 336/1995 (Implementation of Council Directive No. 91/670 on mutual acceptance of personnel licences for the exercise of functions in civil aviation)
Regulation on licensing, No. 419/1999 with subsequent amendments
Regulation on aircraft interception, No. 450/1999
Regulation on the Civil Aviation Board, No. 377/2003
Notice No. 5/2005, regarding safety management systems for ATM service providers
Regulation on the applicability of common rules in the field of civil aviation and the establishment of a European Aviation Safety Agency, No. 612/2005

Source: The Icelandic authorities.

[140] WTO document TN/S/O/ISL/Rev.1, 14 June 2005.
[141] Icelandic Civil Aviation Administration online information. Available at: www.caa.is.
[142] Amendment to Aviation Act 1998 (73/2002) and regulation 377/2003.

135. Foreign ownership in Icelandic companies involved in airline operations may not exceed 49%.[143] This limitation does not apply to nationals of the EEA, who are treated as Icelandic nationals[144] (see Chapter II(4)). Moreover, no undertaking may be granted an operating licence unless it is effectively controlled by EEA nationals (as provided by Council Regulation (EEC) No. 2407/1992). Non-EEA and non-EFTA citizens and companies must obtain a permit to own real estate in Iceland (see Chapter II(3)). There are no limitations on foreign participation in auxiliary services.

136. The Icelandic authorities noted that the Aviation Act mirrors the European legislation, and cabotage is accordingly permitted to EEA operators. Cabotage by non-EEA operators is not permitted unless allowed under the conditions of a bilateral agreement.

137. Security and landing fees are specified in Act 74/2000 and Act 88/2004. As noted in Iceland's previous Review, air fares were liberalized in 1997.

138. During the review period, new bilateral agreements have been signed with a number of parties outside the EEA: China (2003); Hong Kong, China (2004); Macao, China (2004); Croatia (2005); and India (2005). In addition, in 2001 an MOU was signed with Canada on scheduled air services. Iceland has initialled but not yet ratified bilateral agreements with: the Republic of Korea, Sultanate of Oman, Kingdom of Bahrain, United Arab Emirates, India, State of Qatar, Mongolia, and Lebanon.[145] The authorities indicate that most of these are open skies agreements.

139. Since 1 June 2005, Iceland has participated, without voting rights, in the Management Board of the European Aviation Safety Agency.[146]

(v) Maritime transport

(a) Main features

140. Due to Iceland's geographical location and reliance on international trade, maritime transport plays a major role in its economy. As acknowledged by the authorities, maritime transport costs to and from Iceland are relatively high on account of the long distances to major markets, the relatively low volumes transported, and relatively low competition on the relevant routes. Practically all (99%) movements of goods and materials to and from Iceland are by maritime transport. There are no domestically flagged cargo ships in Iceland. Efforts have been made to encourage the registration of cargo vessels in Iceland, by changes to legislation allowing cargo ships to be registered on a dry lease agreement as well as the removal of stamp duty. According to the authorities, however, these efforts have not engendered any results.

141. The volume of goods transported by sea increased from 4 million tons in 2000 to 4.98 million tons in 2003; the biggest increase was in the aluminium harbours. This included 3.2 million tons of imports and 1.8 million tons of exports.[147] Cabotage, however, has continued to diminish. At the end of 2004, the last costal ship bringing cargo around the island terminated its service. While there is no scheduled service, cargo ships call in at major exporters, such as fish processing factories, in various

[143] Law on Foreign Investment in Companies No. 34/1991.
[144] EU regulation 2407, implemented by notice 439/94.
[145] Icelandic Civil Aviation Administration online information. Available at: http://www.caa.is.
[146] European Aviation Safety Agency online information. Available at: www.easa.eu.int.
[147] Statistics Iceland (2005).

harbours around the island. Practically all other cargo is now transported by road to and from Reykjavik.[148]

142. Iceland has 57 ports; 15 have appreciable cargo activities of which three can handle ships up to 40,000 DWt.[149] The rest were built for fishing vessels, but may receive merchant vessels, on an irregular basis, for exports of fish-based products. According to the Icelandic authorities, good natural harbours are available for development in parts of the country earmarked for industrial development.[150] Reykjavík and adjacent ports (Akranes and Grundartangi) serve as the principal import and export points for the country. In 2004, these three ports merged to become Associated Icelandic Ports, which is jointly owned by the local authorities in the area. Reykjavík handles more than 70% of loaded containers, an annual turnover in 2004 of 228,419 TEU of loaded containers.[151] Other important ports are Hafnarfjördur, Akureyri, Vestmannaeyjar, Fjarðabyggð, Þorlákshöfn, and Ísafjörður.

143. In the Uruguay Round, Iceland made no specific commitments in maritime transport services, except that MFN and national treatment were bound for all transport services, and commitments were also made on rental/leasing services without operators relating to ships.[152] Iceland participated in the Extended Negotiations on Maritime Transport Services, suspended in 1996. Although most participants withdrew their conditional offers, Iceland requested that its offer[153] be made an integral part of its GATS Schedule of Specific Commitments.[154] Iceland's commitments in this area extended to cabotage, auxiliary services, customs clearance services, container station and depot, maritime agency services, freight forwarding services, and additional commitments in pilotage, towing and tug assistance, navigation aids, shore-based operational services essential to ship operations, anchorage services, and container handling, storage, and warehousing. In this regard, Iceland is the only WTO Member to date who has scheduled a binding commitment on cabotage.

144. In 1995, the Icelandic authorities provided further details on the market and regulatory structure of Iceland's maritime transport services in responding to a Questionnaire on Maritime Transport Services.[155] Iceland did not propose conditional changes to its maritime transport services commitments in its initial and revised offers in the context of the Doha Development Agenda.[156]

(b) Institutional and legislative developments

145. As specified in the Icelandic Maritime Administration Act (38/1997) maritime transport falls under the responsibility of the Ministry of Transport and Communications. The Icelandic Maritime Administration (IMA) supervises the implementation of maritime, harbour, and lighthouse issues. The IMA represents Iceland in a number of international agencies, including: the International Maritime Organization (IMO); the International Association of Lighthouse Authorities; and the Permanent International Association of Navigation Congresses. It takes part in EEA/EU meetings and is responsible for implementation of the Paris Memorandum of Understanding on Port State Control. As a result of a EEA Joint Committee decision in June 2003, Iceland has the right to be

[148] Ministry of Transport (2005).
[149] Iceland Export Directory online information. Available at: http://www.icelandexport.is.
[150] Invest in Iceland Agency, Doing Business in Iceland.
[151] Associated Icelandic Ports online information. Available at: http://www.faxafloahafnir.is.
[152] WTO document GATS/SC/41, 15 April 1994.
[153] WTO document S/NGMTS/W/27, 24 June 1996.
[154] WTO document S/L/29, 12 September 1996.
[155] WTO document S/NGMTS/W/2, 21 October 1994.
[156] WTO document TN/S/O/ISL, 4 April 2003 and WTO document TN/S/O/ISL/Rev.1, 14 June 2005.

represented, but not to vote, on the Board of the European Maritime Safety Agency.[157] The Minister of Transport and Communications and the General Director of the IMA are advised by a Harbour Council on harbour matters and costal protection, and by a Maritime Council on maritime matters and matters concerning lighthouses.

146. New legislation adopted over the review period includes a new Port Act introduced in 2003 (61/2003). As a result of this Act, a common fee scale applied to all Icelandic ports was abolished. Ports, which are de facto the property of the community in which they are located are now free to set their own fees. According to the Ministry[158], the fees charged by individual ports have not changed much as a result of the Act, apart from at the port of Reykjavik.

147. The Icelandic Maritime Administration charges a lighthouse fee which is used for aid to navigation. According to the authorities this fee relates to the size of the vessel with the same fees being levied on foreign and Icelandic vessels.

148. The State, *inter alia*, provides support for structural repair work, the building of protection barriers, and the deepening of harbours. In 2004, the State provided support of just over ISK 1 billion (US$15.7 million) for such work.[159] State assistance will be reduced after 1 January 2009. According to the Icelandic authorities, a reduction in support will mainly affect the bigger ports, while support for smaller ports might increase.

149. The Act on Maritime Safety, introduced in 2004 (50/2004), accompanied by regulations on Cargo Security (529/2004) and Security Check Procedures by Port Authorities (550/2004), is aimed at protecting ships, crews, passengers, cargo, and port facilities against any kind of terrorist threat or other illegal activities. The Act, which is in accordance with the IMO International Code for the Security of Ships and Port Facilities, involves Icelandic port authorities conducting security assessments and formulating security plans, designating Port Facility Security Officers, training and educating security personnel, and formulating guidelines and standards. At the end of 2005, 29 port security assessments and security plans had been validated, inspected, and awarded a Statement of Compliance of a Port Facility by the IMA and the National Commissioner of the Icelandic Police. The Act on Maritime Safety allows ports to collect a fee on goods, ships, and passengers to cover the costs involved in tightened security (Article 9).

150. As described in the Secretariat Report for Iceland's previous Review, under a national security agreement between Iceland and the United States, an exception to MFN treatment is granted to all incoming and outgoing liner cargoes destined for and originating from the U.S. military forces stationed in Iceland. Tenders for the transport requirements of U.S. Military Sealift Command are open for bids only to Icelandic and U.S. shipping companies. The lowest bidder receives two thirds of the cargo, and the lowest bidder from the other country is allocated the remaining third. Icelandic bidders are not required to employ Icelandic flag vessels.

151. Port services are provided to foreign and nationally owned vessels on a non-discriminatory basis. No ports involved in international traffic are closed or restricted for entrance of vessels owned or operated by foreign nationals. Agency services are provided by all Icelandic merchant shipping

[157] The EFTA Secretariat online information. Available at: http://secretariat.efta.int/Web/News/EMSA/view.

[158] Ministry of Communications online information. Available at: http://www3.samgonguraduneyti.is/radherra/raedur-og-greinar/nr/761.

[159] Fjárýola Ríkisins online information. Available at: http://www.fjarsysla.is/rbh/rbh.nsf/Files/Rikisreikn-04/$file/Rikisreikn04.pdf.

companies, and by several independent agencies and brokers in Reykjavík and other main ports. An agency fee scale is published regularly.

152. Other legislation related to maritime transport can be found in Table IV.7.

Table IV.7
Maritime transport-related legislation currently in force in Iceland, 2006

Acts
Certification of Masters and Desk Officers serving on board Icelandic Ships, Act No. 112/1984 (amended)
Certification of Marine Engineers serving on board Icelandic Ships, Act No. 113/1984 (amended)
Act on the Registration of Icelandic Ships, No. 115/1985
Maritime Act, No. 34/1985
Fishermen's Act, No. 35/1985
Act on Crews Serving on Board Icelandic Passenger Ships and Cargo Ships, No. 76/2001
Ship Survey Act, No. 47/2003
Port Act, No. 61/2003
Act on Maritime Security, No. 50/2004
Act on Ship Safety Monitoring, No. 41/2003
Act on Maritime Accident Investigation, No. 68/2000
Certification of Masters, Desk Officers and Marine Engineers serving on board Icelandic Ships Regulation, No. 118/1996 (amended)
Regulation on Watchkeeping Arrangements on Board Icelandic Passenger Ships and Cargo Ships, No. 599/2001
Regulation on life boats operated from land, No. 123/2003
Regulations on Crews Serving on Board Icelandic Passenger Ships and Cargo Ships, No. 416/2003
Regulation on the survey and power rating of main engines in Icelandic ships, No. 610/2003
Regulation on the Operating Procedures of Accredited Bodies Performing Ship Inspection, No. 94/2004
Regulation on the safety of fishing vessels of 15 metres in length overall and over, No. 122/2004
Regulation on cargo security, No. 529/2004
Regulation on security check procedures by port authorities, No. 550/2004

Source: The Icelandic authorities.

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