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Taking its place in Europe – Iceland's long road to its EU application

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ABSTRACT

Iceland applied for EU membership in 2009. Before that it had sought to alleviate pressures on her to fully integrate with Europe firstly by pursuing limited integration through membership of the European Free Trade Association (EFTA) and later by joining the European Economic Area (EEA). This paper traces the steps taken by this peripheral European country from itsstruggle of independence from Denmark, through World War II, American occupation, the founding of a republic, NATO membership and the Cod Wars with Britain. The paper analyses the various phases of the debate on the ties to the European institutions leading to EEA and Schengen membership, the "miraculous economic success" which ended in the epic crash of 2008 which precipitated a much contested EU application

Introduction

Iceland applied for EU membership on16 July 2009. That ended a long road towards an application from this small peripheral European country that had resisted fully integrating with the EU for almost half a century. In the meantime, Iceland had adopted almost all the main obligations of integration through the deepest cooperation framework the European Union has with any third country: the European Economic Area (EEA). Just like Norway, Liechtenstein, and, after a long and arduous process, Switzerland, Iceland has also joined Schengen, and is thus more deeply integrated with the Union in that domain than some EU countries such as Britain and Ireland.

The membership application started a new process, that has, because of the political situation in Iceland, the potential of becoming relatively dramatic. In fact, it is something of a miracle that it is happening in the first place, considering that only one of the five parties represented in Iceland's parliament, the Alþingi, in the 2009-2013 parliamentary term, supports it and views EU membership positively. Also, according to opinion polls, Icelanders do not seem to have warmed up to the idea of joining the Union. In the last three years opposition to membership averaged between 60-70 percent of voters.[1]

This paper attempts to describe the long road towards Iceland's EU application in the light of Icelandic nationalism, the interests of its leading sectors, the political landscape and ponders the difficulties facing the final stages of this process.

The making of a modern state

The genesis of Iceland's struggle for independence‖ has sometimes been traced to the writings of Eggert Ólafsson (1726-68), a naturalist, poet and royal official, whose ideas of the preservation of the Icelandic language and exaltation of the Icelandic "Golden Age" blended well with the romantic ideals of nineteenth-century nationalists. But nothing could have been further from Ólafsson's mind than wishing for some form of independent Icelandic state. On the contrary, he was a staunch royalist, who ardently believed in the benefits of belonging to the Danish crown , to

[1] Capacent Gallup, (2012), *Viðhorf almennings til ESB,* Reykjavík, Capacent.

which Iceland had belonged for several centuries.[2]

During the 1830s and 1840s a nationalist paradigm shift took place among the Icelandic student community in Copenhagen. The new perspective was based on the belief that the rule of one nation over another was in principle unnatural and had thus to be averted.[3] The students and scholars participating in the debate were influenced by nationalism which had gripped Europe during that century leading to the creation of the nation-states we are familiar with today. From the latter half of the nineteenth, to the first half of the twentieth century, Iceland gradually gained independence from Denmark in a few successive steps: in 1845, a resurrected parliament, the Alþingi, convened for the first time in Reykjavík; in 1874, Iceland received its first constitution, giving the Alþingi limited legislative power and responsibility for the Icelandic budget; in 1904, it was granted Home Rule, with a minister of Icelandic affairs residing in Reykjavík and responsible to the Alþingi; in 1918, the Act of the Union, by which Iceland was declared a sovereign state sharing a monarch with Denmark[4] and finally, the founding of the Republic of Iceland on the 17 June 1944.

On the economic front, following the difficulties in the second half of the 19th century, which saw emigration to America grow significantly, a strong economic upswing occurred in the first three decades of the twentieth century due to the introduction of new fishing techniques and the modernization of the infrastructure including the building of bridges, roads and telecommunications systems and the founding of banks and other financial institutions.[5] The period 1912-30 was described as the most revolutionary period of the Icelandic economy.[6] Iceland's route to economic development followed the textbook model on how small states adapt to the international economy – by exporting one or two main goods according to their comparative advantage. In Iceland's case it was fish.[7]

The Effect of World War II

On the 10 May 1940, British troops occupied Iceland. The Americans gradually replaced the British in 1941, and then in 1942 about 50,000 soldiers were stationed in Iceland, most of them around Reykjavík. During the first years of occupation, there were more British and American than Icelandic men in Reykjavík.[8] Unemployment in Reykjavík, which had been significant before the war, was eradicated in the first months of the occupation,[9] as the occupying forces struggled to upgrade the Icelandic infrastructure, building airports and roads and preparing to defend the country in the event of a German invasion.[10] Iceland, which in 1939 was heavily indebted, managed

[2] Hálfdanarson, G. (2006), 'Language, Identity and Political Integration. Iceland in the Age of Enlightenment', in H. Gustafsson, & H. Sanders (eds.), *Vid gränsen. Integration och identiteter i det förnationella Norden*, Gothenburg, Makadam and Centre for Danish Studies, the University of Lund, pp. 230–247.

[3] Ibid., p. 241.

[4] Hálfdanarson, G. (2001a), 'Icelandic Nationalism: A Non-Violent Paradigm?', in G. Hálfdanarson, & A. Isaacs (eds.), *Nations and Nationalities in Historical Perspective*, Pisa, Edizioni Plus, p. 7.

[5] Jónsson, G. (2002), 'Hagþróun og hagvöxtur á Íslandi 1914-1960', in J. H. Haralz (ed.), *Frá kreppu til viðreisnar; Þættir um hagstjórn á Íslandi á árunum 1930-1960*, Reykjavík, Hið íslenska bókmenntafélag, p. 14.

[6] Magnússon, M. S. (1985), *Iceland in Transition; Labour and socio-economic change before 1940*, Lund, Ekonomisk-Historiska Föreningen, p. 89

[7] Jónsson G. 2002, pp. 15-7

[8] Bernharðsson, E. Þ. (1996), Blórabögglar og olnbogabörn, *Sagnir*, 17. ár, p. 12

[9] Icelandic Government (2007), *Landsframleiðsla og þjóðarframleiðsla 1945-1990*, website of the Icelandic Government at www2.stjr.is/frr/thst/rit/sogulegt/index.htm#5 (viewed in: July 2007).

[10] Snævarr, S. (1993), *Haglýsing Íslands*, Reykjavík, Heimskringla, p. 43

during the five years of occupation, to become one of the wealthiest nations (per capita) in Europe.[11]

Icelandic Nationalism triumphed after World War II following the successful struggle for independence, and attempts at bringing Iceland into Western security cooperation were strongly resisted by nationalist forces, fearing the loss of the benefits of independence.[12] During the war, Iceland had acquired the support of the United States, and President Franklin D. Roosevelt had declared when Sveinn Björnsson, the first Icelandic president visited the White House in August 1944 that the US would after the restoration of world peace, recognize and work for the complete independence Iceland.[13] The American motive was not altogether altruistic, since the US had begun to see the benefits of maintaining a military presence in this strategically situated island in the North Atlantic.[14]

When the American authorities asked for permission to maintain a military base in Iceland, this put pressure on Icelandic politicians to take security issues seriously. Voters' opposed this proposal since a declaration of permanent neutrality had been an element of Iceland's sovereignty since 1918.[15] After the war and with the advent of the Cold War, it dawned on the Icelandic authorities that neutrality was not sustainable. The American military left the country and the government started working towards an agreement, which, among other things, ensured traffic of American aircraft through Iceland's international airport in Keflavík. An agreement was signed in the autumn of 1946. From an Icelandic standpoint, the purpose of the agreement – although not explicitly stated – was to maintain the economic prosperity of the war years.[16]

In between1948-50, Iceland's foreign trade was mainly with Britain and the US. Although the Icelandic government accepted the first payment of Marshall aid reluctantly, its reluctance vanished quickly. Icelanders soon earned a name for being the greediest of all for aid, though they were not very keen on loans. The Marshall Plan helped to close the annual trade gap, subsidized exports to Europe and provided large sums for the development of infrastructure.[17] The aim of the Americans was to acquire a permanent base in Iceland. In the meantime they made sure that Bjarni Benediktsson, the Foreign Minister at the time and later leader of the Independence Party, understood that their financial aid depended on communists being kept out of government.[18]

Nationalist rhetoric instigated the first political riots in the history of the Republic when on 30 March 1949, the Icelandic parliament met to ratify Iceland's membership of NATO. The police and reserves used batons and tear gas to disperse the crowd.[19] But since Iceland had no intention of having its own army, many Icelanders welcomed US military protection so that in the parliamentary vote, 37 voted for membership and 13 against.[20] In 1951 Iceland

[11] Whitehead, Þ. (1991), *Leiðin frá hlutleysi 1945-1949*, Saga, tímarit Sögufélags, p. 64

[12] Kristinsson, G. H. (1991), ‚Iceland', in H. Wallace (ed.), *The Wider Western Europe*, London, Pinter, p. 160

[13] Franklin Delano Roosevelt, quoted in Kristjánsson, S. (2001), *Forsetinn og utanríkisstefnan*, Ný saga, tímarit Sögufélags, 13. árg., pp. 4-16.

[14] Kristjánsson, 2001, p. 12

[15] Whitehead, 1991, p. 112

[16] Ibid., p. 72

[17] Ibid., p. 81

[18] Ibid.

[19] Whitehead, Þ. (2006), *Smáríki og heimsbyltingin; Um öryggi Íslands á válegum tímum*, Þjóðmál, haust, pp. 66-8

[20] Harðarson, Ó. Þ. (1998), *Public Opinion and Iceland's Western Integration*, a paper submitted at the Conference on the Nordic Countries and the Cold War: International Perspectives and Interpretations, June 24-27, Reykjavík, p. 3

signed an agreement with the US guaranteeing Iceland's defence. A military base was later set up close to the airport at Keflavík.

The first years of the republic were also turbulent in economic terms. An urgent need was felt to renew production facilities and overcome housing shortages and, partly under the influence of a strengthened labour movement, more emphasis was placed on direct investment, mainly in the fishing industry. The prosperity of the war years did not change the Icelandic government's mind set towards their sectoral policy. They continued to support the basic industries, fisheries and agriculture, as best they could. Though they understood that agriculture could not spearhead the island's economic development, they believed in its export potential.[21] The foreign-currency reserves accumulated during the war were exhausted in two years.[22] This set the stage for Icelandic economic policy for a decade and a half. Although this approach might have been in line with the prevalent economic thought at the end of the war, later, when the Western world began dismantling protectionist barriers and liberalising trade, Iceland headed in the opposite direction going as far as to maintain an exchange rate for its currency which benefited the fishing industry at the expense of other economic sectors – in short, a textbook example of what economists call "the Dutch disease"[23]. In the years 1948-52, GDP suffered a yearly contraction of c. 3% and did not regain its 1947 level until 1954.[24]

Early moves towards European integration

The cornerstone of Icelandic foreign policy from the founding of the republic was to secure full and undisputed control of the fishing resources on its continental shelf. This objective loomed large in all efforts to join any form of European cooperation.[25] Thus, even though Iceland had participated fully in an effort to establish a free-trade association between the six nations forming the EEC and the rest of the OEEC nations in 1957-58, when discussions started to form EFTA, Iceland (together with Greece, Spain, Ireland and Turkey), was not invited to participate. The obvious reason was the serious dispute with Britain at the time over Iceland's extension of its fishing limits to twelve miles.[26] Another reason is that EFTA was mostly intended as a free-trade area for industrial goods, and only to a very limited extent for agricultural and fisheries products. With the exception of the fishing industry, Iceland had not really developed industrial production of its own. Its economic policy, which had been dogged by state intervention and restrictions on imports, was also such that it would have been inconceivable for it to become a founding member of EFTA.

[21] Jónsson G. 2002, p. 26

[22] Whitehead, 1991, p. 78

[23] Daníelsson, J., & Zoega, G, (2009), *Hagkerfi býður skipbrot - Skýrsla Gylfa Zoega og Jóns Daníelssonar*, Website of the University of Iceland (Háskóli Íslands) at http://www.hi.is/files/skjol/felagsvisindasvid/deildir/hagfraedi/2008_2009/Hagkerfib___ur_skipbrot.pdf (viewed on 24.03.2009). The term ―the Dutch disease comes from the fact that the Netherlands experienced major shifts in domestic production following the discovery of substantial gas deposits in the 1960s. As the exports of this natural resource boomed, the guilder appreciated in real terms, thereby squeezing the profitability of other exports, especially manufactured goods (Sachs, J. D. and F. B. Larrain (1993), *Macroeconomics in the Global Economy*, Prentice Hall. pp. 668-9).

[24] Icelandic Government Website, 2007

[25] Benediktsson, E. (2003), *Iceland and European Development, A historical review from a personal perspective*, Reykjavík, Almenna bókafélagið, p. 47

[26] Gíslason, G. Þ. (1993), *Viðreisnarárin*, Reykjavík, Almenna bókafélagið, p. 199; Ólason, Ó. K. (2002), "Politically impossible", EFTA-umsókn í kjölfar þorskastríðs, in E. H. Halldórsdóttir (ed.), *2. íslenska söguþingið, 30. maí - 1. júní 2002* (pp. 426-35). Reykjavík: Sagnfræðistofnun Háskóla Íslands, Sagnfræðingafélag Íslands, Sögufélag, pp. 426-35.

In 1959 a new government, consisting of the conservative Independence Party and the Social Democratic Party, started to rethink Iceland's attitude towards joining the EEC. In the 1960s this coalition, referred to as the Government of Reconstruction (*Viðreisnarstjórnin*), took major steps to open up the economy. The government followed closely what was happening in the EEC. A committee was appointed in 1961 (*Nefndin um fríverzlunarmál)* to look into the possibility of Iceland joining EFTA in order to strengthen its bargaining position with the EC on free trade in fish. The committee recommended that Iceland should apply for membership of EFTA and negotiate an adaptation period and several exemptions, even if it foresaw the eventual merger of EFTA and the EEC[27]. Many serious obstacles hampered Iceland's attempt to join EFTA and Icelandic officials were made aware of this especially by the British.[28] Following the Cod War of 1958-61, the UK was very reluctant to let Iceland join EFTA.[29] Nevertheless, Iceland pressed ahead by lobbying the other Nordic countries. Iceland's possible membership of EFTA was discussed by EFTA in June 1961.[30] As part of this approach to EFTA, the Government of Reconstruction was also aiming to reduce trade relations with Eastern Europe, which were significant at the time, and to increase trade with Western Europe and the US.

At the end of July 1961 it was becoming clear that EFTA and the EC would not merge, and that Britain and several other EFTA states would seek to join the EC. The Minister of Commerce, Gylfi Þ. Gíslason met the social partners in Iceland several times in August 1961 to discuss the issue. These meetings concluded in a resolution in which all the social partners' organisations, except for the Icelandic Confederation of Labour (ASÍ), stated their support for an Icelandic application for membership of the EEC. These 15 organisations included the Farmers' Association, the Federation of Icelandic Fishing Vessel Owners (LÍÚ), and other organisations of the fishing industry.[31] The Farmers' Association, however, soon retracted its support, since substantial doubts had arisen amongst farmers on the merits of EC membership.[32] In the summer and autumn of 1961 the government seriously considered three options: membership of the EEC, associate membership of the EEC, though no one really knew what this would entail and, thirdly, a customs agreement with the EEC.[33] The main strategy was to ensure that Iceland would retain influence on matters of vital concern to it within the Community. Gíslason toured European capitals in 1961 to discuss Iceland's position with European leaders and the European Commission in Brussels.[34] That trip and further contacts by the Icelandic government showed that most European statesmen considered Association with the EC or a customs union as the best choice in the circumstances[35] a position also favoured by Iceland.[36]

The government thus decided to apply for an Association Agreement with the EEC,[37] but all

[27] Thorhallsson, B., & Vignisson, H. T. (2004), The first steps, Iceland's policy on European integration from the foundation of the republic to 1972, in B. Thorhallsson (ed.), *Iceland and European integration, on the edge*, London, Routledge, p. 25.

[28] Benediktsson E., 2003, pp. 94-6

[29] Ólason, 2002, pp. 434-5

[30] Morgunblaðið, (1961, June 28), 'Aðild Íslands að EFTA rædd', *Morgunblaðið*', Reykjavík. p. 1

[31] Morgunblaðið, (1961, August 18), 'Samtök meginatvinnuvega Íslendinga styðja: Inntökubeiðni í Efnahagsbandalagið', *Morgunblaðið*, p. 1.

[32] Thorhallsson & Vignisson, 2004, p. 27

[33] Gíslason, 1993, p. 201

[34] Ibid., p. 203

[35] Ibid., p. 204

[36] Benediktsson E. 2003, p. 106

[37] Thorhallsson & Vignisson, 2004, p. 27

efforts stopped when Britain's application was vetoed by De Gaulle. Iceland did not revive the issue until 1967.[38] However, it featured in the 1963 national election campaign, with emphasis on the question of sovereignty and the different fisheries policies of Iceland and the EEC.[39] The battle lines were drawn between government and opposition, with the socialist People's Alliance strongly appealing to nationalistic sympathies followed to a lesser extent by the Progressive Party.[40]

Joining EFTA

The Icelandic government began to re-examine EFTA membership in order to pull the country out of the severe economic downswing that had taken hold during the second half of the 1960s. It was intended to help revive other industries apart from the fishing industry. But reaching an agreement with the EC on lower tariffs on fish exports was still perceived as a key priority.[41] There were also worries that Iceland's position in Nordic co-operation was under threat since this had practically been taken over by EFTA after its inception.[42] Also, government officials noted a significant change in EFTA towards Icelandic membership[43] and the British themselves had even, as part of a strategy to strengthen EFTA, proposed bringing Iceland and Ireland into the association.[44] The process of joining EFTA was formally launched in December 1967 with the appointment of a committee of all parties represented in the parliament, which extensively consulted the social partners and organisations representing fisheries, agriculture, industry and commerce.

The Icelandic parliament voted to apply for membership of EFTA on 12 November 1968.[45] A small protest took place outside the Parliament while the vote was being taken and some, alleged to be young socialists, broke a few windows.[46] The socialist newspaper *Þjóðviljinn* however claimed the demonstration was peaceful.[47]

Iceland joined EFTA in March 1970. In 1972 it concluded negotiations on a Free Trade Agreement (FTA) with the EC (together with the other EFTA countries) comprising a significant lowering of tariffs on fish exports. Until 1971, Icelandic political elites had been deeply divided on closer ties to Western Europe, some holding them to be unnecessary, further arguing that Iceland should not participate in supranational organisations, since this would weaken its sovereignty and independence and give foreign companies the opportunity to run businesses in Iceland. The People's Alliance categorically opposed any participation in Western European economic organisations, and the Progressives took a "wait and see" position. The Opposition criticized the government depicting the free trade agreement with the EC as a betrayal, an agreement laying the ground for full EC membership. The government considered Iceland's membership of EFTA as a necessary step for the good of the Icelandic economy, and did not think it would weaken sovereignty.[48]

Agricultural sector interest groups had supported EFTA membership, but changed

[38] Gíslason, 1993, p. 204

[39] Benediktsson E. 2003, p. 109

[40] Thorhallsson & Vignisson, 2004, p. 28

[41] Snævarr, S. (1993), *Haglýsing Íslands*, Reykjavík, Heimskringla, p. 356

[42] Thorhallsson & Vignisson, 2004, p. 29

[43] Benediktsson E., 2003, pp. 118-9

[44] Thorhallsson & Vignisson, 2004, p. 28

[45] Ibid., p. 30

[46] Morgunblaðið (1968, November 13), 'Samþykkt með 35 gegn 14', *Morgunblaðið*, p. 2

[47] Þjóðviljinn, 13 November. (1968, November 13), 'Ákveðið að Ísland tengist hagsmunafélagi auðríkja', *Þjóðviljinn*, p. 2

[48] Gíslason, 1993, p. 215

their position in 1969. It has been argued that the close connection between these interest groups and the Progressive Party was the main reason for this policy change despite the relatively good terms that had been negotiated on increased exports of lamb to the other Nordic countries. Interest groups representing industry were always strongly in favour of EFTA membership, even if it could be argued that in the short run, the most severe impact of membership would be felt by the country's industrial sector.[49]

The Government of Reconstruction finally lost its majority in 1971. But in spite of their serious opposition to EFTA in parliament, the Progressive Party and the People's Alliance took no measures to leave EFTA when they, together with the Union of Liberals and Leftists, eventually formed a government.[50] Lúðvík Jósepsson, the new Minister of Commerce and leader of the People's Alliance, took over responsibility for the country's relations with EFTA, pursuing the path previously taken by Gíslason. The political consensus was that since the country had already joined EFTA, membership was to be supported actively.[51]

Iceland unilaterally extended its fishing limits in 1972 to 50 miles and again in 1975 to 200 miles. These moves were fiercely resisted by Britain, which had fished in these waters for a long time. Britain dispatched naval vessels to guard its fishing boats in the disputed waters. The Cod Wars delayed full implementation of the free trade agreement with the EC until Britain eventually recognized the 200-mile fishing limit.

The effect of the Cod Wars on the Icelandic psyche should not be underestimated. The nationalist rhetoric was unleashed, especially between 1972-3, against the British naval presence in the waters claimed by Iceland. Opposition to NATO and Western cooperation increased.[52] Ingimundarson argues that at this time, two nationalist currents met and merged: traditional western nationalism, based on 19th century ideals and anti-western, third-world type nationalism that can arise when a great power (Britain) is seen to be jeopardizing the future and the economic independence of a small nation. Anger was directed at Britain, as the enemy, the US for not protecting Iceland, the international tribunal in The Hague for siding with Britain and at the other Nordic countries for not standing up for Iceland.[53]

The EEA

After joining EFTA, closer involvement in European integration was not considered necessary in Iceland or the other Nordic countries except Denmark, since the free-trade agreements between the EC and the EFTA states which took effect in 1973 had led to a quadrupling of the volume of trade between EFTA and the EC in the period 1972-86.[54] This, however, led to increasing pressures, especially since the EC member states were deepening their integration, and in the late 1980s the EFTA countries' diplomats in Brussels were beginning to express their worries to the EC Commission, that they were being left out of the dynamic internal market that was due to be achieved by 1992.[55] On 17 January 1989, while addressing the European

[49] Thorhallsson & Vignisson, 2004, p. 32

[50] Gíslason, 1993, p. 215

[51] Benediktsson E. 2003, p. 133

[52] Ingimundarson, V. (2001), *Uppgjör við umheiminn, íslensk þjóðernishyggja, vestrænt samstarf og landhelgisdeilan*, Reykjavík, Vaka-Helgafell, p. 21

[53] Ibid., pp. 340-1

[54] Pedersen, T. (1994.), *European Union and the EFTA Countries*, Pinter Pub Ltd, p. 23

[55] Benediktsson E. 2003, pp. 168-72

Parliament in Strasbourg, Commission President Jacques Delors proposed a new, more structured partnership for the EFTA countries comprising common decision-making and administrative institutions. This was to become the European Economic Area, (EEA) negotiated between EFTA and the EC in 1989-92.

The EEA had first been mentioned in 1984 in the European Council's Luxembourg Declaration, which was the result of an EC-EFTA ministerial meeting held in Luxembourg in April of that year. It mentioned several ways of clearing trade barriers between the two organisations and to promote competition. But Delors' 1989 declaration went further than what was originally proposed in 1984. Delors also wanted to tell the EFTA countries that it would be impossible for them to join the EC, not at least until after the completion of the internal market in 1993.[56]

Joining the EC was also hampered by the neutrality of Sweden, Finland, Austria and Switzerland. But the EFTA countries reacted positively to Delors' proposal. To the neutral countries, neutrality was still incongruent with EC membership, since most EC member states except Ireland were all in NATO, while Norway and Iceland which were in NATO perceived the benefits of improving their access to the European markets without surrendering much of their cherished sovereignty.[57] Delors' Declaration proved unsuccessful in fending off EC applications from the EFTA countries, and Austria became the first one to apply for EC membership on July 1, 1989. Austria's application immediately raised some difficult questions on the compatibility of neutrality in international affairs with the EC's efforts to strengthen cooperation in foreign policy and security.[58]

The EEA negotiations were described by one of the European Commission's chief negotiators as the most complex that the EC had ever been involved in. The EFTA countries had to adopt, on the internal market alone, approximately 1,400 existing EC acts, covering over 10,000 pages of legislation. Time and again, the negotiations were bogged down by disputes over issues ranging from fishing rights, alpine trucking and financial support for the EC's poorer members. The agreement was finally signed on October 22, 1991, only to see its proposed EFTA-EC court declared to be in contravention of EC law by the European Court of Justice. Renewed negotiations ended in a compromise in February 1992.[59]

The Icelandic government at the start of the negotiations on the EEA agreement was made up of a coalition of parties led by the Progressive Party, with the party leader, Steingrímur Hermannsson, as Prime Minister. The other coalition partners were the Social Democratic Party led by Jón Baldvin Hannibalsson who held the Foreign Ministry portfolio and the People's Alliance led by Ólafur Ragnar Grímsson (later President of Iceland) as Finance Minister. Elections were due in 1991, but during the campaign both the Progressive Party and the People's Alliance criticised the EEA negotiations.[60] The Independence Party, which in opposition under the leadership of Þorsteinn Pálsson had been in favour of bilateral negotiations with the EC on fisheries, rather than focusing on the EEA,

[56] Stephensen, Ó. Þ. (1996), *Áfangi á Evrópuför*, Reykjavík, Háskólaútgáfan, p. 30

[57] Ibid., p. 31

[58] Dinan, D. (1999), *Ever Closer Union, An Introduction to European Integration*, Basingstoke, Lynne Rienne, p. 163.

[59] Ibid.

[60] Thorhallsson, B. (2008), Evrópustefna íslenskra stjórnvalda: Stefnumótun, átök og afleiðingar, in V. Ingimundarson (ed.), *Uppbrot hugmyndakerfis; Endurmótun íslenskrarutanríkisstefnu 1991-2007*, Reykjavík, Hið íslenska bókmenntafélag. p. 79.

elected Davíð Oddsson as leader during the campaign and he seemed more positive towards the EEA Agreement and European integration in general. Hannibalsson believed that Oddsson was a liberal Europhile and this strongly contributed to the formation of a new government consisting of the IP and the SDP in the spring of 1991 under Oddsson's leadership, with Hannibalsson continuing as Foreign Minister.[61] The EEA negotiations for Iceland went on unhindered and on 2 May 1992 the agreement was signed in Porto, subject to approval by the individual national parliaments.[62]

In parliament, as in the negotiations on EFTA accession, the position of the political parties depended roughly on whether they were in government or not. Ironically, the same parties that had fought for, and concluded, Iceland's EFTA accession, namely the Independence Party and the Social Democratic Party, were now negotiating its entry into the EEA while the Progressive Party, the People's Alliance, and the Women's Alliance which were in opposition opposed it. Ratification took place on 12 January 1993 with thirty-three members in favour, 23 against and seven abstentions.[63]

Digesting Europe: From EEA to EU application

Following the ratification of the EEA Agreement, Icelandic Europhiles celebrated victory. The Foreign Minister, Hannibalsson, became increasingly positive towards following other Nordic applicants into the European Union. At its 1994 Congress, his Social Democratic Party adopted a position that Iceland should apply for EU membership as soon as possible. Later that year Norwegian voters rejected EU membership which meant that the EEA would somehow survive. Unfortunately for them, during the 1995 Icelandic electoral campaign, the negative vote in Norway prevented the Icelandic social democrats from gaining more support for their membership proposal.[64] For domestic political reasons, the Social Democrats performed very poorly, receiving about 11 per cent of the vote. The party had split, with a popular vice-chairman and government minister, Jóhanna Sigurðardóttir, founding her own party[65] which received more or less the support that the SDP had lost. The government retained a majority of only one parliamentary seat. The Prime Minister, Davíð Oddsson, decided to swap coalition partners and the Progressive Party replaced the Social Democratic Party in government with Oddsson's Independence Party.[66] After the ratification of the EEA Agreement, Oddsson became increasingly sceptical towards the EU, and definitely did not share Hannibalsson's enthusiasm for membership. The EEA issue had been difficult for the IP and the party leadership saw it as the furthest step that Iceland could take in the European integration process for three reasons – it was sufficient as a method of ensuring the country's commercial and economic interests; secondly, further integration might harm the interests of the fishing industry, and thirdly, it was a means of avoiding a full-blown split within the Independence Party on EU matters.[67] Thus the new government removed the EU membership issue from the political

[61] Ibid., pp. 80-3

[62] Hannibalsson, J. B. (1992, August 20), *Speech, introducing the EEA agreement to Alþingi, the Icelandic Parliament*, Website of Alþingi at www.althingi.is/altext/116/08/r20125029.sgml (viewed on: 21.07.2009).

[63] Alþingistíðindi 1992-93 (1993), *Alþingistíðindi 1992-93, hundraðasta og sextánda löggjafarþing*, Reykjavík, Alþingi, p. 5964.

[64] Kristinsson, G. H. (1995), 'The Icelandic Parliamentary Election of 1995', *Electoral Studies*, p. 333.

[65] Ibid., p. 334

[66] Ibid., p. 335

[67] Thorhallsson, 2008, p. 111

agenda while stressing the unacceptability of the EU's fisheries policy and that all the country's vital economic interests were adequately protected by the EEA Agreement.[68] In 2002, Oddsson told a meeting of the German-Icelandic Chamber of Commerce in Berlin, that had Iceland not concluded the EEA Agreement, it would have joined the EU "a long time ago".[69]

The discussion on EU membership remained relatively dormant until 1999–2000, when there was a brief surge in enthusiasm for membership driven by the fact that Iceland's opportunity to influence legislation within the EEA was restricted to the preparatory stages and that this was unsustainable. The main argument was that Iceland should seek EU membership so as to be in a position to influence European legislation, the majority of which is automatically incorporated into Icelandic law on the basis of the EEA Agreement.[70] Also, at the time, Iceland was becoming deeply involved in the Schengen scheme and began full participation in it on 25 March 2001.[71] The main reason behind Iceland's joining Schengen was its participation in the Nordic Passport Union, which had been formed by Norway, Sweden, Finland and Denmark in 1957 and which Iceland had joined in 1965. When Denmark decided to join Schengen, it did so with a proviso stating that its decision was subject to the condition the Nordic Passport Union would continue to exist. This eventually led to all the Nordic countries joining Schengen, both the EU and non-EU countries (Norway and Iceland).[72] The Icelandic government was initially lukewarm about joining Schengen. Oddsson was sceptical. However, the issue enjoyed broad support with all parties in the Alþingi, with the exception of the Left Greens, who argued that it was costly and seemed to be just another step towards EU membership.[73]

National Security

National security issues have not been relevant to the question of EU membership, since the defence agreement with the United States and Iceland's NATO membership provided plentiful security without EU membership.[74] However, in the first decade of the twenty-first century, things took an unexpected turn. On 15 March 2006, the US deputy-secretary of state, Nicholas Burns, announced in a telephone call to Iceland's Foreign Minister, Geir H. Haarde, that the US would withdraw all its jet fighters and helicopters from Iceland by the end of September 2006 and severely reduce the US military presence.[75] In reaction, Iceland's prime minister, Halldór Ásgrímsson, suggested that this might provide a reason for Iceland to look seriously into the EU membership option as a guarantee of the country's security.[76] On 30 September 2006, just six months after Burns' phone call to Haarde, the last US soldier left Iceland.[77] Since then, the Icelandic

[68] Ásgrímsson, H. (2000), *Skýrsla Halldórs Ásgrímssonar utanríkisráðherra: Staða Íslands í Evrópusamstarfi*, Reykjavík, Utanríkisráðuneytið, pp. 249-68

[69] Arnórsson, A. (2009), *Inni eða úti? Aðildarviðræður við Evrópusambandið*, Reykjavík, Háskólaútgáfan, p. 123.

[70] Einarsson, E. B. (2009), *"Hið huglæga sjálfstæði þjóðarinnar"Áhrif þjóðernishugmynda á Evrópustefnu íslenskra stjórnvalda, doktorsrannsókn*, Reykjavík, Háskóli Íslands, pp. 261-8

[71] Eiríksson, S. (2004), 'Deeply involved in the European project; Membership of Schengen', in B. Thorhallsson (ed.), *Iceland and European Integration, on the edge*, London, Routledge, p. 50.

[72] Ibid., pp. 51-2

[73] Thorhallsson, 2008, p. 100

[74] Thorhallsson, 2008, p. 127

[75] Mbl.is, (2006, March 16), *Allar þyrlur og herþotur verða fluttar á brott í haust*, Website of Mbl.is at http://mbl.is/mm/gagnasafn/grein.html?grein_id=1071916 (viewed on: 21.07.2009).

[76] Mbl.is, (2006, April 11), *Varnarmálastefna ESB í mótun', 11, viewed*, fWebsite of Mbl.is at www.mbl.is (viewed on 05.31.2006).

[77] Visir.is. (2006, September 30), *Herinn er farinn*, visir.is at http://www.visir.is/herinn-er-farinn/article/200660930059 (viewed on: 07.02.2013).

authorities have taken over responsibility for running the air patrols over Iceland and Icelandic waters. Several defence agreements have also been concluded with neighbouring NATO countries, under which they provide air patrol services.[78] However, the defence agreement with the US still stands and this explains why the US withdrawal has not had a significant impact on the attitude of the Independence Party towards EU membership.[79]

"God bless Iceland"

For a long time after the founding of the republic, foreign investment was viewed with suspicion and through nationalistic eyes, with the fear that foreigners would buy up Iceland. This fear was unnecessary since, except for heavy industry, where the selling point has been cheap energy, Iceland has always found it difficult to attract foreign capital into its businesses.[80] What might have been viewed by foreign investors as Iceland's most lucrative investment opportunity, the fishing industry, is subject to severe restrictions on foreign investment.[81] Foreign direct investment did not follow automatically after Iceland joined the EEA: no multinational companies set up branches in a country with fewer than 300,000 inhabitants, with its own tiny currency that tended to fluctuate wildly. Even when the banks were being privatised at the turn of the century, efforts to attract foreign buyers were to no avail. However, soon after the beginning of the twenty-first century, this began to change dramatically, with Icelandic FDI inflows far surpassing the EU average. Two factors in particular account for this: firstly, a huge investment in a new aluminum smelting plant in the east of Iceland and secondly, investment in the financial sector.

Unfortunately most of the investment in the financial sector was actually done by Icelanders themselves through their companies abroad.[82] Moreover, the country's status as a stable, European, democratic and prosperous country was reflected in its ratings by international agencies, such as Moody's and Standard & Poor's. This meant that Icelanders' access to international loans was almost unlimited. Thus, a generation of ambitious Icelandic businessmen set off to create their own multinationals.[83]

It has been claimed that the biggest single factor in making this development possible was Iceland's participation in the European Economic Area.[84] Icelandic businessmen, however, claimed that they were more risk-prone and quicker to make decisions than their European counterparts.[85] Unfortunately this level of risk-taking did not pay off in the end. On the 6 October 2008 following serious turmoil in financial markets worldwide, the government of Iceland introduced emergency legislation empowering it to take over the entire Icelandic banking system.[86] Prime Minister, Geir H. Haarde, addressed the nation

[78] Gísladóttir, I. S. (2008, April), *Skýrsla Ingibjargar Sólrúnar Gísladóttur utanríkisráðherra um utanríkis- og alþjóðamál*, Website of Icelandic Ministry for Foreign Affairs at http://www.utanrikisraduneyti.is/media/Skyrslur/Skyrsla_um_utn_april_08.pdf, p. 18 (viewed on: 02/07/2009).

[79] Thorhallsson, 2008, p. 128

[80] Jónsson, Á. (2009), *Why Iceland?*, London, McGraw Hill, pp. 86-7

[81] Haraldsson, G., & Magnússon (eds.), M. Á. (2009), *Ísland 2009, stöðuskýrsla*, Reykjavík, Félagsvísindastofnun Háskóla Íslands, Hagfræðistofnun Háskóla Íslands, p. 48

[82] Ibid., p. 50

[83] Jónsson, (2009), pp. 86-7

[84] Sigfússon, Þ. (2005), *Straumhvörf, útrás íslensks viðskiptalífs og innrás erlendra fjárfesta til Íslands*, Reykjavík, Mál og menning, p. 75

[85] Harðardóttir, H., & Ólafsson, S. (2007), *Hröð ákvarðanataka í íslenskum útrásarfyrirtækjum*, Reykjavík, Viðskiptafræðistofnun Háskóla Íslands, p. 3

[86] Alþingi, Þskj. 80 — 80. mál. (2008, October 6), *Frumvarp til laga um heimild til fjárveitingar úr ríkissjóði vegna sérstakra aðstæðna á fjármálamarkaði o.fl.*, Website of Alþingi at http://www.althingi.is/altext/136/s/0080.html (viewed on: 2/07/2009).

on radio and television to explain the gravity of the situation, concluding his address with the words "God bless Iceland", which are not often heard from Icelandic politicians. Suddenly, Iceland changed from a rich and successful state with a growing financial infrastructure, banks and businesses that had made their presence felt in international markets, into an international pariah for its reckless financial behaviour.[87]

Within a week after the Prime Minister's address some 85% of the banking sector collapsed, together with the Icelandic currency, the *króna*.[88] The Icelandic stock market, in which the nominal value of stocks had increased nine-fold from the beginning of the privatisation of the banks until their peak in 2007, took a nosedive. The index went from 9,016.5 points on 18 July 2007 to 218.8 on 8 April 2009. Between 26 September 2008 and 14 October of the same year it went down from 4,277.3 to 678.4.[89] On 24 October the Icelandic government asked the International Monetary Fund (IMF) to intervene to re-establish financial stability.[90]

In connection with the fall of Landsbanki, and to protect its 300,000 British depositors, the UK government resorted to the "Landsbanki Freezing Order 2008", by which all Landsbanki assets in Britain were frozen. To do this the UK government resorted to the Anti-terrorism, Crime and Security Act, which had been enacted in the wake of the September 11th attacks on the US and had never been used before against a Western state. For 24 hours, the Central Bank of Iceland and the country's Ministry of Finance were also under this Act, in company with entities such as Al Qaeda, the Taliban, North Korea and Zimbabwe. This was interpreted by many Icelanders as an act of aggression against the country.[91] It vividly exposed the country's vulnerability in the international order and gradually developed into the worst dispute Iceland had landed itself in since the financial crash began – the so-called Icesave affair.

In the Icesave dispute Britain and the Netherlands sought to exact interest payments from Iceland for the money these countries decided to pay out to British and Dutch depositors after the fall of Landsbanki. In order to force Iceland to pay, they used their positions within the board of the IMF to delay emergency payments to Iceland during the worst phase of the crisis. On two occasions Iceland reached agreement with the British and Dutch governments on the payments, just to see the agreements overturned by Icelanders in referenda held at the initiative of the Icelandic president, Ólafur Ragnar Grímsson. Finally, the EFTA Surveillance Authority (ESA) brought the case to the EFTA Court in December 2011, arguing that Iceland had acted in breach of the Deposit Guarantee Directive by failing to ensure the payment of a minimum compensation of EUR 20.000 per depositor,[92] and the European Commission led the prosecution. However, Iceland was cleared of all charges by the Court and on 28 January

[87] Jóhannesson, G. T. (2009), *Hrunið*, Reykjavík, JPV , pp. 262-9.

[88] Matthiasson, T. (2009), 'Spinning out of Control, Iceland in Crisis', *Institute of Economic Studies Working Paper Series*, p. 1.

[89] M5.is. (2009, April 14), *M5.is - Miðpunktur atvinnulífsins*, Website of M5 (a stock market website at http://m5.is/?gluggi=visitala&visitala=13 (viewed on: 14.04.2009)

[90] International Monetary Fund, (2008, October 25), *Iceland: Request for Stand-By Arrangement - Staff Report; Staff Supplement; Press Release on the Executive Board Discussion; and Statement by the Executive Director for Iceland*, 2012, International Monetary Fund: http://www.imf.org/external/pubs/cat/longres.aspx?sk=22513.0 (viewed on 10.25.2012).

[91] Jóhannesson, 2009, pp. 180-1

[92] EFTA Surveillance Authority (2013, January 28), *Internal Market: Statement concerning judgment in the Icesave case | EFTA Surveillance Authority*, Eftasurv.int at http://www.eftasurv.int/press--publications/press-releases/internal-market/nr/1842 (viewed on 08.02.2013)

2013, the case was dismissed. The EFTA Surveillance Authority is supposed to pay its own costs and the costs incurred by Iceland, which were significant, while the European Commission was ordered to pay its own.[93]

This affair damaged the EU's reputation in Iceland, which was perceived as siding with and helping Britain and the Netherlands against Iceland.

To help Iceland find its way out of the crisis many alternatives were mentioned, in early 2009 in the wake of the financial crash, such as EU membership and adoption of the euro. The exceptional circumstances created by the crash, and the public unrest which followed, led to the collapse of the government and snap parliamentary elections in the spring 2009. As a result the parties that were willing to support an EU membership application obtained a parliamentary majority. These parties were the Social Democratic Alliance, the Civic Movement, and the Progressive Party (even though the Progressive Party spelled out strict preconditions for it in its election agenda). However, the "historic" opportunity to form the first left wing majority government in the history of Iceland, led to a formation of government consisting of the Social Democrats and the (Eurosceptic) Left Green Movement. It was with the clear understanding that the government would pursue an application for EU membership as soon as possible with the aim of concluding negotiations for entry into the union, which would then be up to the population of Iceland to accept or refuse in a national referendum. The Left Greens also stressed their prerogative to be against a concluded accession treaty. After five weeks of deliberations by the Alþingi's Committee on Foreign Affairs and a week of heated debate in the Alþingi itself, Iceland applied for membership of the European Union on 16 July 2009.

Conclusion

It took fifty years from the first hesitant steps by the "Government of Reconstruction" towards European integration to the application for membership of the European Union in 2009. As the discourse in Iceland shows, although the application was not inconceivable, it would probably have taken more deliberations for further years or decades, had it not been for the unparalleled economic crash Iceland experienced in 2008 and the serious political turmoil it created in 2009. The outcome of the application procedure is far from certain. With general elections due in April 2013 and the parties opposing membership flying high in the opinion polls, it is possible that the application will simply be withdrawn later on this year, as happened in the case of Switzerland in 1992.[94]

At least since the early 1960s, Iceland has been under pressure to participate in the European integration process. This pressure came from a number of sources, from increasing interdependence on the international stage and regional integration in Europe. As the Liberal intergovernmentalists claim, the EU has turned out to be a successful intergovernmental regime designed to manage economic interdependence through negotiated policy co-ordination, which created economic incentives for peripheral European states to join the process. There have, however, been limits to the depth to which Iceland has been prepared to go at any given stage.

[93] EFTA Court (2013, January 28), *Judgment of the Court - (Directive 94/19/EC on deposit-guarantee schemes – Obligation of result – Emanation of the State – Discrimination)*, from Eftacourt.int at http://www.eftacourt.int/images/uploads/16_11_Judgment.pdf (viewed on 08.02.2013).

[94] Dinan, 1999, p. 168

Certain options were available to Iceland relating to its geopolitical position and history. Thus, Iceland had the possibility of integrating gradually, without taking on the full obligations of EU membership. Majority governments in Iceland have always been coalition governments and until 2009 these always included either the Independence Party or the Progressive Party, both of which had extensive links with sectors that were sensitive to integration and felt threatened by it. The fact that the party that has most vocally opposed integration with the EU – the Left Greens – supported (or let through) an EU Membership application can be explained by the fact that the agricultural and fishing lobbies are not strongly represented in it.

The sensitive domestic constraints in Iceland facing European integration are particularly related to the position of the fishing industry and to a lesser extent agriculture. The direct connections between two of Iceland's parties, the Independence Party and the Progressive Party, which have served in government for the longest periods in Iceland's political history, and the fisheries and the agricultural sectors, obstructed moves towards an openly positive stance on EU membership within these parties, particularly in the Independence Party. It has thus been able, due to Iceland's proportional-representation voting system, to block moves towards EU membership, at least until 2009, when the way was cleared for an application because for the first time in the history of the republic, the two parties with the most extensive connections with the fishing industry and agriculture were not represented in a majority government. If Iceland successfully negotiates EU membership, then the power of the leading sector will be tested in a national referendum.

As of now Iceland is negotiating its entry into the EU. Out of 33 chapters, 27 have been opened and 11 concluded (in February 2013). The most difficult chapters, amongst them fisheries and agriculture, will not be opened before the general elections in April. It is for a new government to decide how to continue with this process. A new Europhile party, "Bright Future" has been getting good results in recent opinion polls, although it seems to be at the expense of the other Europhile party, the SDA. The Independence Party is adamant that if it enters government it wants a referendum on whether to continue the negotiating process or not, while the SDA argues that such a referendum would be "on nothing of worth", since no one would know how a final accession agreement would look like. In the meanwhile, nationalist rhetoric might ride high again. The coming months are once again crucial for Iceland's EU application.

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