

The Role of Iceland in the International System as a Small State and the Issue of European Union Membership

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Abstract

This study discusses the role of Iceland -which declared its independence from Denmark in 1944- in the international system and the causes that led the country to withdraw its European Union candidacy in 2015. This country, considered as one of the Scandinavian countries, has in fact its own unique structure. This unique structure has its roots in Iceland's history, its determination about protecting the elements of national identity, geographical-climatic characteristics and economic factors such as the fishing industry. Iceland, which is the only NATO member without an army, has been through Cod Fish crisis' with England, and the Ice-Save crisis with England and the Netherlands. The country, which had an important economic crisis in 2008, has shown a more positive attitude about EU as the government has also changed, however with the end of the crisis and another change of government, it has once again opted for a self-sufficient strategy. The country, which became member of the European Economic Area (EEA) in 1994 and of European Free Trade Area (EFTA) in 1970, aims to conduct political and economic relations through territorialisation or bilateral relations instead of participating to a big integration model or developing multilateral relations. Iceland's primary foreign policy objectives throughout the new century seem to secure full control over its territory (land and waters), improve market access for its fisheries products and guarantee its defense. Although the governments varied from time to time, all political parties subscribed to the same goals though they differ on how to achieve them. Arctic issue seems to gain importance also for this country in 2010s.

Keywords: Iceland, European Union, Small power, Small state, Arctic

Introduction

The late independence of Iceland, which remained under Danish sovereignty until 1944, has affected negatively the participation of the country to international organizations, especially concerning the European Union or its integration to Europe because Iceland has aimed, first of all, to become a strong, self-sufficient country in the matter of national sovereignty. Iceland has joined the European Free Trade Association in 1970 and has joined the European Economic Area in 1994. The coming into force of the Schengen Agreement in 2001 has developed the relations of Iceland with the member states of the EU. Furthermore, the economic crisis of 2008 has changed the structure of national politics and has led to a considerable back down on the cautious politics against the union. The country, with the influence of the economic crisis, has officially applied for membership in 2009. For Iceland, which is at least as sensitive as Norway, especially about fishing policies, this step has been taken as a result of the international conjuncture. The country, while desiring to be a part of the integration, has never been really enthusiastic about membership. The economic crisis in Europe in 2009 and the austerity measures that came with, have greatly affected Iceland and the confidence on EU membership has been shaken. Iceland, which put on hold the membership negotiations after the general elections of 2013, has officially withdrawn the EU membership application in March 2015. One of the main reasons of this decision is the various political parties that came to power in the country. The landscape of EU membership has changed after the Independence Party and the Progressive Party from the right wing have built a coalition and have come to power in the 2013 general elections.

Access to new transport routes in the north and the discovery of previously unknown natural resources and oil and gas reserves due to the melting of the glaciers in the Arctic; caused by the global warming, has increased Iceland's geostrategic importance once again. Furthermore, the country is an important trade partner for Europe in the economic area as well. In

this study, which will focus especially on the issue of Iceland's EU membership, at the same time, the country's foreign policy priorities, crisis' and its role in the international system will also be addressed. Thus, the importance of Iceland in the system as a small state, which is generally known for its hot springs and fishing policies, will be analyzed.

Iceland at a Glance

Iceland, a small island country of approximately 103.000 km², located in the north of the Atlantic Ocean, seems at first glance, to be very different from the other European countries due to its geographic situation and climate, and also seems to stay apart from them on identity and cultural matters. This observation is in fact not completely incorrect. The country, whose closest neighbor is Greenland, has close historical ties with Norway and Denmark. However, it has many differences even with these two Scandinavian countries. Iceland, generally speaking, is a one of its kind, "unique" state.

The island discovered in 9th century by Norwegians, has first been settled by Vikings coming from the same country. Althingi, which is also the actual name of the parliament, has been founded during the Viking era and has been the oldest and highest institution in the country up to the present day. The parliament founded in 10th century, though it was different from the political institutions of present day, is an important demonstration of Iceland's efforts for being a democratic country, even in that era. The island lost its independence in 13th century and remained under the domination of Norway, its neighbor located 1050km away. When Norway formed the Kalmar Union with Denmark, it has come under Danish reign. The Kalmar Union also covered Sweden, the Faroe Islands, the Orkney Islands and the Shetland Islands and continued to exist until the first quarter of 16th century. ¹

The dependence on the Kingdom of Denmark has continued after the 1st World War; the country has declared its independence only in 1944. The declaration of independence has been accepted without a violent reaction by Denmark, which was under Nazi occupation. Iceland, which has not been through great and bloody wars in its past has also managed to protect itself from armed conflicts during the 2nd World War. "There is a tendency to ignore the international environment which triggered various steps which led to full independence. The independence struggle is seen by many Icelanders as having been won by national unity built on Icelandic culture and uniqueness ably led by distinguished national heroes."² Although the independence process has heroes like Jon Arason, Jon Sigurosson, Iceland is not a country where the "big leader" concept is in the showcase. For example, Iceland's history does not have a hero, warrior or savior such as Gengis Khan who is a legend in Mongolia and also in the world.

The late independence is in fact directly related to the withdrawal of the European Union candidacy of Iceland, which is the subject of the present study. There are obviously multiple reasons for the withdrawal of the candidacy and they will be discussed in the study, however the first and foremost reason is the late independence of Iceland. Dependence on a foreign entity or participating to a great integration model has always been considered as plan B by this country where the national identity and sovereignty notions are very strong. The country has usually tried to build its foreign policy on bilateral relations and has not made any compromise in subjects that bear vital importance for itself, like the fishing industry. As it will be discussed later, even economic crisis' or changing governments have not affected said policies. This attitude can be subject to criticism in an international system where cooperation gains more and more importance, however the behavior of a small island state that chose to determine its own destiny, to be self-sufficient, can also be seen as a successful strategy. Iceland occupied a geopolitically strategic position during the Cold War. Iceland has a special security experience and it is related to the important location of Iceland in the middle of the GIUK-gap (Greenland, Iceland, UK) in the Cold War.³ The country which, during the Cold War had an important place especially for NATO, has lost its significance in 1990's. However the melting of the glaciers in the Arctic caused by the global warming and the discovery of previously unknown natural resources, oil and gas reserves, access to new transport routes show that the country can become geopolitically significant once again.⁴ "The scramble for the Arctic has revived the Northern dimension – Icelandic Arctic discourses now play on the

¹ Baldur Thorhallsson, "Iceland's contested European Policy: The Footprint of the Past – A Small and Insular Society", *Jean Monnet Occasional Papers*, No.1, Malta, Institute for European Studies, 2013, p.5.

² *ibid.*

³ Baldur Thorhallsson, "The Distinctive Domestic Characteristics of Iceland and the Rejection of Membership of the European Union", *European Integration*, Vol.23, 2001, p.276.

⁴ Selin Güler, Azra Ayata, "İzlanda'nın Avrupa Birliği'ne Üyelik Sorunsalı", 31 July 2014, p.1.

<http://www.bilgesam.org/incele/1727-izlanda%E2%80%99nin-avrupa-birligi%E2%80%99ne-uyelik-sorunsali/>

prospects of a renewed strategic relevance in a future Great Game, wrought by the impact of climate change in the region.”¹

A Special Case of Small State

Small states, which mean states that have a small land area, can seem in the first glance to be in disadvantage and weaker compared to great powers. While the extension of the state borders brings endless advantages to countries in terms of power, it can also cause never-ending problems. Small states may have strategic importance especially on a regional scale, even though they cover a small area. A small state can also be a much stronger decision maker compared to other countries possessing larger lands.

In the international relations discipline, the definition of small state and which countries can be considered as small states is open to discussion. Notions like small state, small power became an important study subject among theoreticians especially after 1990's and many different views have been formulated. Europe, where Iceland is located, is rich in countries that can be considered small states. From Benelux to Baltic countries, including Balkans and Switzerland, many European States are accepted as small states. Iceland is one of the small states in Europe as well. To further deepen the subject within the discipline, Iceland can even be considered as a small island state.

One of the most important theoreticians about small states is Peter Katzenstein. Katzenstein had greatly contributed to the literature about small states theories with his book named "Small States in the World Markets"² written in 1985. His work still serves as reference to numerous studies. Katzenstein has taken as basis 7 countries while naming the main characteristics of small states; Sweden, Norway, Denmark, the Netherlands, Belgium, Austria and Switzerland. As his work has been adapted to various countries by theoreticians, it has also been applied to Iceland. "The question is: how well does the theoretical framework of SSWM travel? Does it still apply a quarter of a century after its inception? In his own revisit of SSWM in 2003, Katzenstein recognized that while he had carefully delimited his investigation to seven early industrializers of the Western core nations (Sweden, Norway, Denmark, the Netherlands, Belgium, Austria, Switzerland), his conclusions could be potentially fruitfully applied and tested in other contexts: "analysis could have pushed further by investigating, in addition, the strategies of other small states situated differently in the world economy"³

According to Katzenstein, Iceland, which can be considered as one of the Scandinavian five, is in fact different from the other countries of the region due to many of its characteristics. Iceland is accepted as a special case in its relations with the EU. In Katzenstein's *Small States in World Markets*, "it maintained that the choices of seven small European states are conditioned by two sets of interlinked forces, that is historically shaped domestic structures and the constraints of the international economy. This is also evident in the case of Iceland – our test case. Past decisions and reliance on international trade still have a profound influence on present political and economic choices."⁴ However, according to Katzenstein, Iceland which has close ties especially with Norway and Denmark among Scandinavian countries, differs from these in 3 ways: Economic openness, corporatist structure and political party systems. In addition to these factors affecting the integration process with EU, Iceland's special security experience, special characteristics of the Iceland administration should also be discussed in relation with the membership problematic.⁵ Before discussing these points, it is also necessary to see how much of a "small state" Iceland considers itself.

In the actual Iceland's political life, the political discourse has not been characterized by a notion of the "little Iceland" contrary of the Danish discourse of the "lille Danmark" (little Denmark). Rather, policy leaders have picked up or dropped the language of smallness according to context. By the late 20th century, it seems that Iceland preferred to define itself as a small vulnerable community. The reason behind this was the political view of that period, according to which in case

(accessed August 2016)

¹ Valur Ingimundarson, "Iceland's Post-American Security Policy, Russian Geopolitics and the Arctic Question", *the RUSI Journal*, Vol. 154, No.4, 2009, p.1.

² Peter J. Katzenstein, *Small States in World Markets – Industrial Policy in Europe*, Cornell University Press, 1985.

³ Vytautas Kuokštis, "Baltic States in World Markets: Does Katzenstein's Framework still hold?", *Journal of Baltic Studies*, Vol.46, No.2, June 2015, pp.109-110.

⁴ Baldur Thorhallsson, "The Corporatist Model and its value in understanding small European States in the neo-liberal world of the twenty-first century: the case of Iceland", *European Consortium for Political Research*, No.9, 2010, p.375.

⁵ Baldur Thorhallsson, "The Distinctive Domestic...", *op.cit*, p.257.

Iceland joined the UN Security Council or the EU, it would not have much of a say in this supranational structure. The opinion that it would not have much political influence in the supranational structures as a small state, has created a negative view in the public opinion and caused that in that period in Iceland, being a "small" state became an "unfamiliar" and even "unwelcome" notion. In other words, Icelanders, because of these arguments formulated in politics, have felt themselves stuck in the portrait of an ineffective country on what concerns the system. However, in 2000's, despite the economic crisis of 2008, this view has changed once again, and Iceland has underlined in politics that, despite being a small state it is a powerful state in many areas. This has been realized in accordance with Iceland's nature and needs.¹ The fact that it withdrew its candidacy in 2015 from a supranational structure like the EU shows indeed that Iceland considers itself important and powerful from the international system point of view, despite being a small state.

In order to understand Iceland's relations with Europe and why at the end it withdrew its candidacy, it is necessary to examine the various factors important to country's domestic and foreign policies. These factors will be examined under the headlines of country's foreign policy and defense priorities, economic drawbacks and political system, in the same order.

General Foreign Policy and Defence Priorities

Iceland's foreign policy and defense strategies can be classified under four main groups which are; NATO membership and defense agreement with the USA, joining the European Free Trade Area (EFTA), joining European Economic Area (EEA) and the "wait and see"² approach concerning the EU. The relations with the USA can be defined as the Atlantic pillar and reflect this country's main security-defense plan. "The functional solution that Iceland has found for its defense is a direct defense agreement with the USA, signed in 1951, combined with Iceland's membership of the North Atlantic Treaty Organization. The US forces stationed at the Keflavik base in south-western Iceland, which form the Iceland Defense Force, are seen as guaranteeing the necessary deterrent and (initial) response capacities for Iceland's protection in a crisis, while in peacetime they provide air defense cover. Iceland has, of course, its own police force, coastguard and emergency rescue services, but it depends a good deal in practice on the US assets at Keflavik even for the function of air-sea rescue. While all the Nordic states have some degree of acknowledged or existential dependence on US military power, Iceland thus represents an extreme case of an 'Atlantic' choice in terms of defense identity and an exceptionally clear rejection of the 'European' choice in terms of joining the integration process."³ The relations with the USA are in fact established on the basis of defense and security and until USA closed the military base in Keflavik in 2006, the security mechanisms that EU membership would bring were not needed. NATO membership and the agreement signed with the USA in 1951 were considered to be sufficient as defense strategy for the only European country without its own army. It's clear that the special relationship between Iceland and USA influences the process of integration to the EU. As long as Iceland has this relationship with the USA, it need not look to European Integration to strengthen its security.⁴ However after 2006, "...Atlantic pillar has however become less important than before, giving more weight to the European cooperation in foreign and security policy matters"⁵

Iceland's quest to position itself within Europe "came first on the agenda by the end of 1957 when leaders in Western Europe were preparing to create a joint forum for the six states in the European Economic Community (EEC) and the other members of the Organization for European Economic Co-operation (OEEC), of which Iceland was a member. After talks broke down in 1959 the UK government lead a group of seven states establishing the European Free Trade Association (EFTA) in 1960 – as an intergovernmental counterweight to the supra national characteristics of the EEC. Iceland's main interests in foreign trade were to insure access for its fish products into European markets – of which the UK was vital. As EFTA was mainly formed around free trade with industrial goods Iceland did not join the association in the beginning. After

¹ Alyson JK Bailes, Baldur Thorhallsson, "Small States: A Theme in Iceland Political Science and Politics", *Nordiques*, No.27, 2014, pp.123-124.

² Kristinsson argues that the cautious approach to European union is "wait and see attitude"
G.H. Kristinsson, "Iceland and the European Union: Non-decision on Membership", in Miles (ed), *The European and the Nordic Countries*, London, Harvester Wheatsheaf, 1996, p.150.

³ Alyson JK Bailes, Baldur Thorhallsson, "Iceland and the European Security and Defence Policy", in Alyson Bailes, Gunilla Herolf og Bengt Sundelius (ed.) *The Nordic Countries and the European Security and Defence Policy*, SIPRE – Oxford University Press, 2006, p.328-329.

⁴ Baldur Thorhallsson, "The Distinctive Domestic...", *op.cit.*, p.262.

⁵ Eirikur Bergmann, *Iceland and the EEA 1994-2011 Rapport*, Europautredningen, 2011, p.8.

the UK applied for membership in the EEC in 1961 the newly formed progressive coalition (SDP and IP) seriously contemplated applying for membership in EEC rather than joining EFTA). The Icelandic government only abandoned the plan of seeking membership in the EEC after the French leader Charles de Gaulle had vetoed the UK's application. Consequently, Iceland applied for membership in EFTA in 1968 and joined in 1970 – accompanying rapid industrialization in the Icelandic economy.”¹ After the industrialization and the EFTA membership that granted easy access to the fish market, a fishing industry crisis with England, named “Cod Wars” took place. This subject will be treated in the economic drawbacks section.

In the beginning of the 1990's EFTA countries and the members of the European Economic Community accelerated the efforts to build the European Economic Area. The advantages and disadvantages of this subject have been widely discussed in the Icelandic parliament. All interest groups composed of the public opinion, syndicates and workers' groups took an active role in government's EEA membership. As a result, Iceland has joined the EEA in 1994. Iceland's EEA membership meant the harmonization of 80% of its national legislation with the EU legislation and it brought along the application of the free circulation of persons, capital, services and goods under the four freedoms headline, within the limits established by the Icelandic Foreign Affairs Ministry. Despite the fact that in 1994 Social Democrats (Alþýðuflokkurinn) had a positive attitude about the EU membership in their electoral campaign, in 1996 the coalition including the Independence Party (Sjálfstæðisflokkurinn) has openly been against EU membership. Nevertheless, Iceland has signed the Schengen Treaties in 1996, due to which border controls with European countries have been terminated. This subject has been a great cause of debate in 2000-2001 in the parliament.²

“Entering into the EEA has resulted in active Europeanization of the Icelandic society and weaving Iceland ever more closely into the European internal market. The EEA agreement has clearly and greatly influenced the development of the Icelandic society. Its impact is not only measured through the legal acts Iceland has had to adopt but also through increased and more informal trans-border cooperation which has followed. The EEA opened up the closed off Icelandic society and provided for a mere transformation in the economy which became much more diversified and increasingly internationalized.”³

The final foreign policy axis to be discussed following Iceland's NATO, EFTA and EEA memberships, is the EU membership process. The process gained momentum with Iceland's full membership application in 2009. The 2008 crisis, which will be discussed in detail in the following section, is a key point for Iceland's application for full membership of EU. A crisis on a scale that was never seen before in Iceland, the collapse of the entire financial sector in one night, had an important role in changing the negative attitude about the EU membership. Additionally, the fact that the coalition, in which the Independence Party suspicious about EU membership, was the biggest partner, lost the elections in April 2009 and that it has been replaced by the coalition government constituted Social Democrats and Left-Green Movement (Social Democratic Alliance - Samfylkingin-Jafnaðarmannaflokkur Íslands) had an important impact on EU membership process. Other political parties that had strong prerequisites about the fishing and farming industries have also supported the EU membership because of the influence of the crisis.⁴ The behavior of these parties will be examined in detail in the final section.

In 2010, the European Commission has expressed a positive opinion about Iceland's EU membership, and the same year, the Council of Ministers has decided to start the membership negotiations. Iceland having a great performance in the negotiations, has successfully concluded 11 of the 27 chapters. The 6 chapters that caused great conflict between Iceland and the EU namely fishing, agriculture and rural development, food safety, veterinary and plant health, settling right and freedom of service, free movement of capital have never been opened to negotiation. Iceland, which in fact advanced very quickly in the process has suspended the relations with the EU in 2013 and temporarily closed the 16 chapters. In Iceland, which froze the EU membership negotiations in 21 May 2013 in accordance with the decision of the coalition government, the anti-EU attitude has been visible in the parliamentary elections as well. The votes of the Social Democratic Alliance fell under 25%, Independence Party and Progressive Party (Framsóknarflokkurinn) which both wanted to conduct the bilateral

¹ *ibid*, p.8.

² Altuğ Günar, “Avrupa Birliği-İzlanda İlişkileri”, in Ercüment Tezcan, et.all (eds), *Avrupa Birliği'nin Doğu Avrupa ve Balkanlar Genişlemesi*, Bursa, Sentez yayınları, 2015, pp.695-706.

³ Eirikur Bergmann, *op.cit*, p.10.

⁴ Selin Güler, Azra Ayata, *op.cit*, p.2.

relations within the scope of the EFTA agreement and which were distant to EU earned the majority of the votes.¹ This new anti EU attitude seen in the public opinion and in the parliament can mainly be explained by the fact that by 2011 Iceland has overcome the 2008 crisis. The country that became relatively confident in the economic area has focused on founding its policy on bilateral or regional relations again and has taken its distances from the idea of being member of a supranational structure. The negotiations that were suspended in 2013 gave way to the full withdrawal of the candidacy in March 2015. "Iceland's interests are better served outside the European Union," the minister wrote on his website. Iceland has said it wants to maintain "close ties and cooperation" with the EU, and indeed already benefits from such links."²

Economic Issues

Katzstein's studies about Small States says that these countries are specialized in their exports. Furthermore, in common with the other small states, due to the small scale of its economy, Iceland is heavily dependent on the import of other goods. Membership of the EEA also contributes to the openness of the economy. Exports in Iceland are concentrated on two big markets European Union and USA. Political parties have been very reluctant to open up the economy because major interest groups have campaigned against it, especially the fisheries and the farmers were the pressure groups.³

It has already been said that Iceland believes its relations with EFTA and EEA to be sufficient, and therefore does not need a supranational structure like the EU. The country, no matter who is in the government, is known for applying very strong policies and not having compromises especially on what concerns the fishing and agriculture industries. Such that, fishing has become a national identity element for Iceland and together with Norway it became one of the two most discussed countries in the system concerning this subject.

Iceland did not only have a hard time in the EU negotiations concerning the fishing, but has gone through crisis' with the United Kingdom as well. 3 different crisis named "Cod Wars" took place between 1961-1975 between these two countries. These 3 crisis' which were based on economic disagreements have been seen as an independence war in Iceland.⁴ "Iceland managed to extend its fisheries zone on a number of occasions, eventually to 200 miles, despite heavy protests from powerful neighbors. This is particularly interesting because of its more limited capabilities compared to Britain, its main opponent. These 'victories' no doubt reinforced Icelandic politicians' view that Iceland could be successful on its own without having to negotiate and make compromises within multilateral international forums. This is not to say that the international environment did not contribute to Iceland's success. On the contrary, the development of the law of the sea was in Iceland's favor and the country's strategic military position played a key role in British decisions to give in on the fishing-zone issue following pressure from the US and other NATO allies".⁵ The main reason England accepted the sea mile limits dictated by Iceland at the end of these crisis, is that it realized the prolongation of the crisis could damage USA's military interests in the island. As a result of the crisis, Iceland has been able to fish in a larger area due to its strategic location during the Cold War, and the level of prosperity in the country has risen.⁶ Iceland's success in the Cod Wars is still considered as legendary in the country. The fact that a small country obtained such a victory against "big states" concerning an industry that was made into a national identity symbol, is one of the greatest sources of pride of the country in foreign policy and shows once again the importance of said industry. "From the Icelandic perspective, the Cod Wars were also about nationalism, Western integration, historical memory and domestic party politics."⁷

The fishing subject has caused many problems in the relations with the EU as well. The industry has been essential since the foundation of Iceland; the surrounding waters which are fed by the gulf waters coming from south create a suitable environment for fish to feed and breed. This industry is important for marine research as well. The fishing industry constitutes the 6% of Iceland's GNP, the country realizes the 5% of the total global fish export. European Union's Common

¹ Altuğ Günar, *op.cit.*, p.697.

² <https://www.theguardian.com/world/2015/mar/12/iceland-drops-european-union-membership-bid> (accessed August 2016)

³ Baldur Thorhallsson, "The Distinctive Domestic...", *op.cit.*, p.264.

⁴ Selin Güler, Azra Ayata, *op.cit.*, p.2.

⁵ Baldur Thorhallsson, "Iceland's contested..", *op.cit.*, p.9.

⁶ Selin Güler, Azra Ayata, *op.cit.*, p.2.

⁷ Valur Ingimundarson, "Fighting the Cod Wars in the Cold War: Iceland's challenge to the Western Alliance in the 1970s", *the RUSI journal*, June 2003, p.90.

Fishery Policy was not in accordance with Iceland's requirements. Also because of the Relative Stability, according to Iceland, the quantity fished in the past should remain the same; the special and traditional structure should continue to exist. Additionally, the country had discords with the EU during the candidacy process, about the quota-hopping, i.e. determining the fishing quotas. A crisis has also taken place between EU and Iceland in 2010, concerning the situation of mackerel fish.¹ Finally, Iceland continues whaling for commercial and scientific reasons and this situation is subject to great protests of environmentalists.²

Like fishing, agriculture is also a controversial negotiation chapter for the Icelandic political elites. During the negotiations, Iceland has claimed that Icelandic farmers should benefit from some exemptions like their Finnish counterparts do, because the country is located way up in the north and farmers are exposed to difficult environmental conditions. Iceland's claims have made the progress under the Agriculture negotiation chapter difficult. If Iceland had become EU member, it would have benefited from the possibilities provided by the Common Agricultural Policy and the rural areas in need would have developed. The farmers could even have directly benefited from the incentives and EU structural funds could have been provided to the rural areas in need. However, from this point of view, the withdrawal of the candidacy has been detrimental to Iceland.

In order to establish a direct relation between Iceland's economy and the European Union candidacy process, it is necessary to discuss the 2008 financial crisis. As a result of this crisis during which the country lived a great economic depression, the EU candidacy process has sped up. The neo-liberal policies introduced by the government since mid 80's, the fast privatization of public properties and the participation of the country to EEA pushed the Icelandic financial sector into a fast growth trend. Because of the fast and uncontrolled growth of the financial sector, the global economic crisis starting in 2008 has caused bigger damages in Iceland compared to other countries. The devaluation of the Icelandic krona has greatly increased the debt of individuals and of private business' which were engaged in loans in foreign currency. Inflation and unemployment have reached unseen levels and the financial sector has collapsed in one night.³ "During this crisis the three largest banks (Glitnir, Kaupthing, and Landsbanki) all collapsed and many other smaller banks and companies went bankrupt in the aftermath of the crisis with severe consequences for the economy and the people. Prior to the crisis, Iceland, a high income OECD economy, had experienced strong growth rates and unprecedented expansion in overseas investment and activities, especially in the financial sector. (...) The collapse of the Icelandic banks in October 2008 was a shock to the Icelandic nation as well as internationally. In fact, it can be said that this was the first time that financial events in a tiny country like Iceland sent shockwaves through the international financial markets."⁴ The never-seen-before financial crisis in Iceland has caused a change in the political decision makers' negative attitude towards EU membership.

Finally, the crisis that needs to be treated under the economy headline is the "Ice-Save Crisis". Iceland has gone through this crisis together with England and Holland in parallel with the 2008 economic crisis. Landsbanki's declaration of bankruptcy due to the economic crisis has prevented the Dutch and English citizens who had accounts in the bank, from having access to their accounts. The payment of the damages caused by this situation has been requested, while the Icelandic parliament voted in favor of the compensation law, the people of Iceland have rejected it in a referendum. The case has been brought to EFTA Court and the Court has reached a decision in favor of Iceland in January 2013. The tension with two countries in addition to the economic crisis has created a negative attitude towards EU in the public opinion. "Ice-save" killed the attraction of the EU accession for a big part of Icelanders as ordinary citizens lost their faith in the European legal order"⁵

¹ Altuğ Günar, *op.cit.*, pp.708-710.

² Selin Güler, Azra Ayata, *op.cit.*, p.2.

³ Baldur Thorhallsson, Rainer Kattel, "Neo-Liberal Small States and Economic Crisis: Lessons for Democratic Corporatism", *Journal of Baltic Studies*, Vol.44, No.1, p.12.

⁴ Hilmar Þór Hilmarsson, "Small States and big banks – the case of Iceland", *Baltic Journal of Economics*, Vol.13, No.1, 2013, pp.31-36.

⁵ Elvira Méndez-Pinedo, "Iceland and the EU: Bitter Lessons after the Bank Collapse and the Ice-Save Dispute", *Contemporary Legal and Economic Issues*, Vol.3, 2011, p.1.

The Policy-Making Process and the Party System in Iceland

In order to understand Iceland's role in the international system and the EU process, it is important to briefly discuss the country's specific political system structure and the views of the political parties.

Icelandic governments historically have built their closest relations with the Scandinavian countries. The historic and cultural ties with Denmark and Norway are quite numerous and in fact the country considers the Scandinavian region as a role model. However, the most important difference between said region and Iceland is the corporatist structure in policy-making in Scandinavian countries, compared to the structure based on cooperation in Iceland. Katzeinsein argues that the corporatism of small states is one the most fundamental characteristics of these states comparing to the larger states. Katzeinsein's small state application is not valid for the Iceland case. The fact that the economy of Iceland is concentrated in one sector (fishery) has not made easier for opponents to reach a compromise and consensus. Inside, there is a conflict-oriented relationship between employers and employees' organizations and the government in Iceland. And the labor market organizations have not been willing to form alliances with each other in order to solve particular problems, thus their relationship is characterized by conflict. The intervention of the state and the political parties in cooperation process between employers and employees are more limited in Iceland than in the other Nordic countries. Conflicts between political parties have added to the lack of consensus in the labor market in Iceland but the EEA agreement has increased cooperation and consultation between different groups. This non-corporatist structure of Iceland did not possess the framework where the issue of EU membership can be discussed.¹

Historically, all political parties have opposed in general to the membership of the EU with the exception of the Social Democratic Party in the period 1994-1999 and the Social Democratic Alliance from 2002. In 2009, the traditionally internationalist and increasingly pro-European Social Democrat party had found themselves in a strong position after their election victory the same year, which for the first time opened the prospect of a majority in parliament for opening EU talks. Indeed, the SDA went so far as to make an EU application a precondition for maintaining its coalition government with the conservative Independence Party after the banking crisis of late 2008, and then for creating a new majority government with the Left Green Movement after the spring elections.²

"The economic crash, which started with the fall of the Icelandic krona in March 2008, clearly stimulated the ongoing EU debate and led to a swift change of attitude towards the vulnerability of the economy and its small currency. The SDA's economic plan for recovery was based on EU membership, emphasizing the benefits for consumers and enterprises of lower prices of goods, the adoption of the Euro within the EU as a bulwark for Iceland's shattered finance system, and opportunities for aid for rural areas, agriculture and the tourist industry from the EU's Structural Funds. The Social Democrats may have captured the opportunity to apply for membership, based on their interpretation of Iceland's economic interests, but despite the shock of the economic crash, other parties have not followed them in their pro-European approach. The Left Green Movement remains steadfast in its opposition to EU membership. It reluctantly became prepared to go along with an EU application in 2009 in order to form a government and have an open, democratic EU debate in the country at large. (...) From mid-2010, two procedural issues have dominated the EU debate. First, Parliamentarians from all parties, except the SDA, have now submitted several motions calling for a referendum on whether the EU negotiations should even be continued, or more simply, for the immediate withdrawal of Iceland's application. So far no action has been taken on these proposals in parliament, showing that the majority there and the government still stand by the continuation of negotiations. The second issue has arisen over the alleged EU pressure on Iceland to 'adapt' its laws and practices to EU norms even before the treaty of accession has been concluded or ratified. The government has had to recognize Left Green concerns on this by promising there will be as little 'adaptation' as possible until a final decision on membership has been taken by a popular vote."³ After the crisis has been overcome in 2011, the process ended with the suspension in 2013 and complete withdrawal of the candidacy in 2015. Historically, Icelandic political elites have adopted the idea of belonging to a supranational structure like EU for a short period. However, it is important to underline that even though the people of Iceland have been more pro-EU than the political elites, most of the time they had doubts also about EU membership.

¹ Baldur Thorhallsson, "The Distinctive Domestic...", *op.cit.*, pp. 267-269.

² Graham Avery, Alyson JK Bailes, Baldur Thorhallsson, "Iceland's Application for European Union Membership", *Studia Diplomatica*, 2011, pp.95-96.

³ *ibid.*

Finally, the fact that in case of EU membership Iceland would be under represented and that its election system gives more representation right to rural areas with low population density can give an idea about why EU membership negotiations have been suspended. Not being represented in EU institutions in the decision making stage despite being a member of EEA and the Schengen Zone and Iceland being bound by the decisions made by EU institutions concerning the common market and the Schengen Zone has strengthened the position of EU supporters. However, on the other hand in the public opinion it has created a negative attitude about the candidacy. In addition to this, according to the country's election system, the citizens from rural areas and having agricultural occupations are more representation right and the high representative ratio in these areas where fishing-agriculture topics are vital has triggered the suspicions about EU since many years. These populations have mostly voted for anti-EU parties.¹ "The electoral system is characterized by an unequal distribution of seats in favor of the rural areas and to the detriment of the capital, Reykjavik. (...) Parliamentarians from the rural areas are therefore less likely to challenge the status quo and support EU application."²

Conclusion

Even though Iceland, which is a part of the Scandinavian five, has been considered as a distant small island state because of its geographic situation, in various periods it had important roles on a regional basis in the international system. Despite the fact that the role of small states is considered to be invisible in the system, Iceland is one of the countries that prove they can be a strong actor in a regional scale. Iceland, which started the EU candidacy process in 2009, had a positive view about the candidacy because of the economic crisis and the changing governments. However, the "wait and see" policy resulted in the complete suspension of the process in 2015. The study has aimed to focus on why the candidacy process has been stopped and on Iceland's role in the system and in the Scandinavian region as a small state.

Today, the interruption of the EU candidacy process is explained by international relations experts by various factors and the international behavior of Iceland can be explained also by an exceptional combination of domestic and international factors. Economic factors; especially disagreements with EU concerning the fishing and agriculture sectors, party policies and the representation issue, lack of corporatism, newly founded independence and together with this, developing national sovereignty and identity elements, special relationship with USA about the defense and security politics, are important variables concerning the end of the candidacy process. The most important of these is without doubt the suspicious approach to the membership of supranational structures in the light of the developing identity topic and national sovereignty caused by the late independence. In fact, being a part of supranational structures like EU always seems advantageous for small countries in theory, however the question has always been a dilemma for Iceland. Icelandic governments usually have a less willing attitude about multilateralism. Iceland believes bilateral relations are sufficient for having a place in the system and is not keen on having economic and political elements managed in a large scale by a supranational institution. The country, which is a member of EFTA, NATO and EEA, considers its ties with said institutions to be sufficient.

In fact, the country cleverly using the advantages generated by 1-2 sectors in which it is powerful, is the proof that small states can have a say in the system by the good use of national factors. Even if it also related on the international conjuncture, Iceland's success in Cod Wars or Ice-Save crisis shows that small states can also be in an advantageous position against larger states. As a matter of fact, today Iceland desires to take things further by establishing a regional structure including the United Kingdom that decided to leave the EU in accordance with the referendum results. "When Britain leaves the EU, we will see a triangle that covers a large part of the globe: Greenland, Iceland, the Faroe Islands, Norway - and now the United Kingdom," Iceland's President Olafur Ragnar Grimsson said in an [interview to Iceland Monitor](#). "It is about trade, diplomacy, commodities and several other fields," Grimsson said, stressing that the Arctic, or the far north, would become more important not only in a European, but in a global context as well."³ We can conclude from these words that the country has shut its doors to EU definitely and wishes to pursue new structures. However, it is important to remember that Iceland which had a favorable opinion about EU after the 2008 crisis, is not entirely safe from the possibility of a future crisis. In addition to this, the future of the defense-security relations with the USA is open to discussion. The country has started to gain geopolitical importance once again because of the melting glaciers in the Arctic region,

¹ Selin Güler, Azra Ayata, *op.cit*, p.4.

² Baldur Thorhallsson, "The Distinctive Domestic...", *op.cit*, p.270.

³ <https://www.rt.com/business/349008-iceland-uk-northern-union/> (accessed August 2016)

however only time will show if it will be able to use this situation in its advantage. Finally, what we cannot deny about Iceland, is that we are talking about a country which has its own personality.

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