

**Directorate for Financial and Enterprise Affairs
COMPETITION COMMITTEE**

Annual Report on Competition Policy Developments in Iceland

-- 2017 --

27-28 November 2018

This report is submitted by Iceland to the Competition Committee FOR INFORMATION at its forthcoming meeting to be held on 27-28 November 2018.

JT03448612

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Iceland

1. Executive Summary

1. The current policy objectives of the Icelandic Competition Authority (ICA) are to make markets work better for the general public and the economy. On the basis of these general objectives, the ICA has developed more detailed objectives for its enforcement and advocacy (chapter 2).
2. In 2017 the ICA experienced a considerable increase in merger notifications, many of the mergers addressing significant changes in important markets. As a result of this, the time allocated to merger cases increased to more than 40%, from around 15% in the preceding years (chapter 3.1 and 4).
3. The ICA blocked two mergers, one between a grocery and pharmaceutical chain and the other in the field of EPS production (Expanded Polystyrene). Several mergers were cleared with conditions through settlements with the merging parties. Most notable of these interventions were extensive conditions that were imposed on a merger in telecoms and media (chapter 3.1).
4. The ICA settled cases in the banking sector and in the postal market, making room for more vigorous competition in these important markets.
5. By employing more stringent prioritisation criteria, the ICA has managed to reduce the number of pending cases considerably (chapter 4).

2. Competition policy and priorities in enforcement and advocacy

6. The ICA's activities are based upon clear policy objectives and priorities. To that end the board of the ICA reviews periodically its policy objectives, taking into account the economic situation at a given time, the indications of competition problems in individual markets, as well as available resources.
7. According to the ICA's policy formulation in 2017, the main policy objectives were to improve the functions of markets for the benefit of the general public and the economy. More precisely, the ICA intends to prioritise the following issues in the coming years:
 - Monitor the developments in the ownership of undertakings, detecting common ownership and other ownership links that can adversely affect competition.
 - Take an active role in discussions on the development of the financial market in Iceland, taking account of earlier experience in the field of competition.
 - Monitor the developments in the groceries market and address problems that may impede new competition.
 - Conclude ongoing investigations into the transport and fuel markets.
 - Continue to advocate for the application of competition assessment in the public sector.

3. Key examples of enforcement and advocacy

8. Following are key examples of the ICA's enforcement and advocacy activities, which were addressed in 2017.

3.1. Merger enforcement

3.1.1. Prioritisation revised due to increased merger activity

9. In 2017 the ICA experienced a considerable increase in mergers addressing significant changes in important markets. As a result of this, the time allocated to merger cases increased to more than 40%, from around 15% in the preceding years.

10. This increase forced the ICA to revisit its prioritisation policies in mid-year 2017. With this in mind the ICA had to issue a public statement in July, announcing that due to the workload with respect to merger reviews, many other cases would be postponed or re-evaluated.

11. The ICA blocked two mergers, one in the dairy and pharmaceuticals sector and the other in the field of EPS production (Expanded Polystyrene). Several mergers were cleared with conditions through settlements with the merging parties.

3.1.2. A merger between the largest retailer and a large pharmaceuticals retailer annulled.

12. In July 2017 the ICA blocked a merger between Hagar, an operator of retail companies, and Lyfja, a pharmaceuticals retailer. Hagar is the largest retailer in Iceland, operating retail chains such as Bónus (groceries) and Hagkaup (groceries, cosmetics, clothes etc.). Lyfja is one of the two largest pharmaceuticals retailers, also an active retailer of cosmetics, hygiene products etc.

13. The ICA underwent a broad investigation that tested its earlier assessments in many areas. For example the merging parties argued that the market situation had changed dramatically since Costco, the internationally operated retailer/warehouse, opened a large warehouse in Iceland two months before the decision. Hagar claimed that this called for a change in the ICA's assessments in earlier cases, where the ICA had found that Hagar were in a dominant position.

14. The merging parties also claimed that the Keflavik Airport Duty-Free Store, which operates stores for both departing and arriving passengers, should be considered to be a part of the relevant market. They also argued that online shopping should be included in the market definition.

15. After an extensive investigation the ICA concluded that Hagar was still in a dominant position that would be strengthened by the merger and that the merging parties were close competitors in the market for cosmetics and hygiene products, the market for vitamins, supplements and minerals and the market for health-related groceries (such as organic and vegan products). Together, they would have held a considerable market share in these markets. It also concluded that the merging parties' arguments regarding KEF Duty Free Store and regarding the relevance of online shopping did not have merit.

16. Thus, the ICA found that the merger would seriously harm competition, as an important competitor (Lyfja) would cease to exist as an independent entity. The ICA also

found that remedies proposed by the merging parties would not address the authority's concerns. For this reason, the ICA annulled the merger.

3.1.3. A merger in Telecoms and Media cleared with extensive conditions imposed.

17. In October 2017, the ICA concluded an investigation of an acquisition by Fjarskipti hf. ("Vodafone") of certain assets of 365 miðlar ehf. ("365 media"). Vodafone provided telecommunication service to its customers in Iceland and is an important player in the market and was active in mobile, landline, television and internet services. 365 media was a leading and a full-scale broadcasting company in Iceland both in television, print, online news and radio. In recent years, it has also offered telecommunication services as a virtual network operator.

18. After comprehensive discussions, the ICA and the parties to the merger reached a settlement, addressing the competition concerns. Firstly, to address the loss of an important player offering bundles of telecommunication and pay-TV services, Vodafone agreed to adhere to detailed conditions that would enable new competition to enter the market, e.g. through wholesale agreements. Secondly, to address the vertical competition concerns, Vodafone committed to offer media companies distribution of TV and radio channels on its network on fair and non-discriminatory terms. Thirdly, to address the high level of common ownership in the relevant markets, behavioural remedies were imposed that aim at guaranteeing the independence of Vodafone's board and its key employees.

19. Fourthly, Vodafone committed to ensure that customers would benefit from efficiencies and positive effects on plurality and diversity that the company claimed would result from the merger. For plurality and diversity reasons, Vodafone also committed to guarantee the continued operation of acquired TV and radio stations, including the newsroom and editorial board, and continued production of Icelandic audio-visual content, for at least three years. Vodafone committed as well to facilitate access for at least three independent domestic TV stations with news and cultural content.

20. The merger is addressed in more detail in the ICA's annual report for 2016.

3.2. Other enforcement activities.

21. Parallel to merger investigations and other extensive ongoing investigations in cartel- and abuse cases, the ICA concluded several investigations into possible breaches of the prohibition rules. It also continued several investigations that are still pending, e.g. an extensive investigation into maritime and land transport. The following concluded cases should be highlighted:

3.2.1. Measures to spur competition in the retail banking market

22. In July 2017, the ICA concluded an investigation into the banking market through settlements with the three largest Icelandic banks, which were all parties to the case. The banks agreed to commit themselves to:

- reduce costs charged to customers when they switch retail banks,
- make it easier and more efficient for individuals and small companies to shop around for financial services and thus exert greater competitive discipline on those offering retail banking services,

- counter conditions that may facilitate tacit collusion in the market for retail banking services.
23. As part of the settlement, the banks commit to adhere to the following conditions in their operations:
- Switching between banks will be facilitated.
 - Switching costs such as repayment fees will not be charged for early redemptions made by debtors in the case of loans that carry variable interest rates, when the borrower is an individual or a small enterprise.
 - Caps on fees will apply in the case of charges for transferring tied private pension savings from the banks to other entities that offer private pension fund management.
 - Swapping of mortgage debtors via property transactions will no longer be conditional upon the buyer moving all of his or her banking services to the respective bank.
 - Customers will be notified of significant changes to interest rates and service fees before they take effect, in order to enable customers to transfer their banking transactions elsewhere, should they choose to do so.
 - The banks will make sure that all information on general fees, rates and terms that are published on the bank's website, is accessible through an open API (application programming interface), available to third parties (individuals, enterprises or associations) for download and to set up comparison websites.
 - Certain contractual rights according to the terms of older mortgage loans, that have significant tying effect in the opinion of the ICA, and which triggered an investigation by the ICA, will not be applied by the bank.

3.2.2. Measures to improve competitive conditions in the postal market

24. In February 2017 the ICA concluded an investigation against the state-owned incumbent postal service company, Iceland Post (IP). The investigation entailed several complaints from market participants, most of them having to do with allegations that IP had been using profits from the state reserved area of its business to cross-subsidise its competitive activities. IP still holds a monopoly for the distribution of letters up to 50 gr. It holds a dominant position in the postal market (for the distribution of postal items weighing up to 2 kg). The case was concluded with a settlement with the IP, where the company committed to conditions that were designed to resolve the identified competition problems. The settlement stipulates the requirement to prepare separate LRAIC-based accounting statements for each of IP's significant business areas that are open to competition and clear criteria is set out for the assessment of potential cross-subsidies from the reserved area to the competing business areas. Furthermore, IP's subsidiaries shall be operationally and administratively independent from IP and that IP's express mail service business will be moved out of the parent company into a separate entity as a subsidiary and certain restrictions regarding IP's transactions with its subsidiaries are introduced.

25. The settlement includes provisions intended to ensure that competitors of IP in the distribution of unaddressed advertising mail can buy distribution from IP in remote areas, at the same cost/transfer price as IP itself. Furthermore, the settlement provides that competitors of IP in the field of postal services should get comparable terms and conditions when they do business with IP, as other customers of the company in equivalent

transactions. Moreover, IP is prohibited (unless there exists an objective justification) to refuse to sell its services to competitors in the area of universal service.

3.3. Advocating for a Competition Assessment.

26. The ICA has run a special advocacy initiative through a series of meetings, held under the heading “*Let’s talk about competition*”. One of the main goals of this initiative is to encourage policymakers and public authorities to adopt the methods of competition assessment, as proposed by the OECD. In February 2017, Ania Thiemann, Head of Global Relations at the Competition Division, was invited to Reykjavík for a series of meetings with ministries, public authorities and other policymakers, to introduce and discuss the methods of competition assessment and what lessons can be learned from earlier experiences worldwide. For this purpose, the ICA organised 12 meetings with some 120 participants in total, representing some 30 different ministries, public bodies and industry associations. These meetings followed an earlier visit by Ms Thiemann, in December 2015.

4. Resources of the Competition Authority

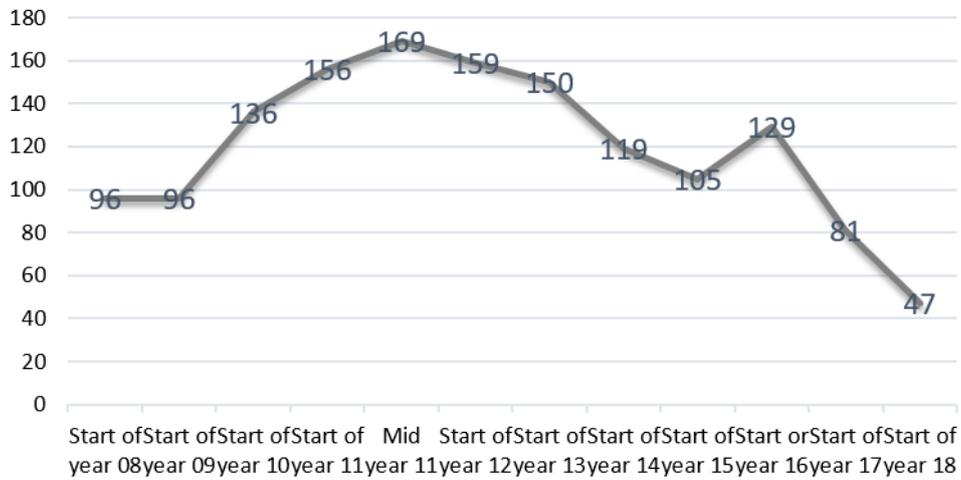
4.1. Budget and pending cases

27. The ICA is funded through the state budget. The budget for 2017 amounted to approx. 3.7 m. EUR (exchange rate as of 1 January 2018).

28. In the previous years, ICA has had to apply rigorous prioritisation in response to an increased workload, that could for a number of years be traced to the banking collapse in 2008, but has recently been due to increased merger activity, not least in important consumer markets (see 3.1.1).

29. In the years 2011 - 2014 and again in 2016 - 2017, the ICA increased the level of prioritisation, bringing the number of cases from 129 at the beginning of 2016, down to 47 in at the start of 2018. By this, the ICA has strived to get at better control of case processing, namely to tighten the criteria for cases that are initiated and brought to conclusion.

Figure 1. Number of pending cases

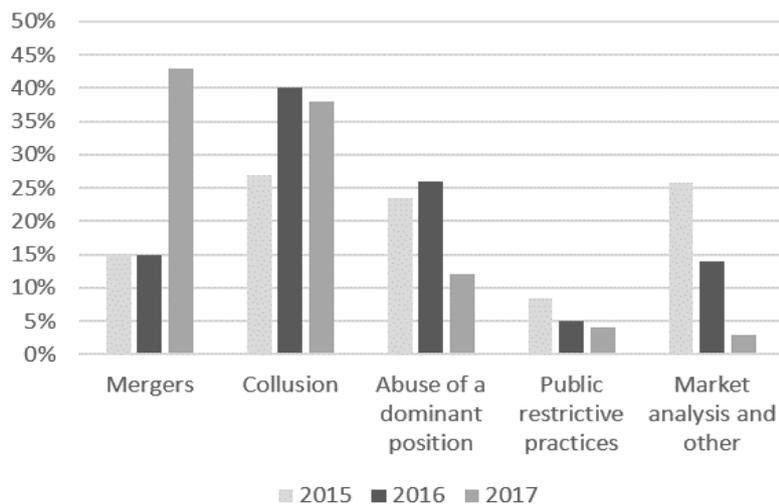


4.2. Allocation of resources

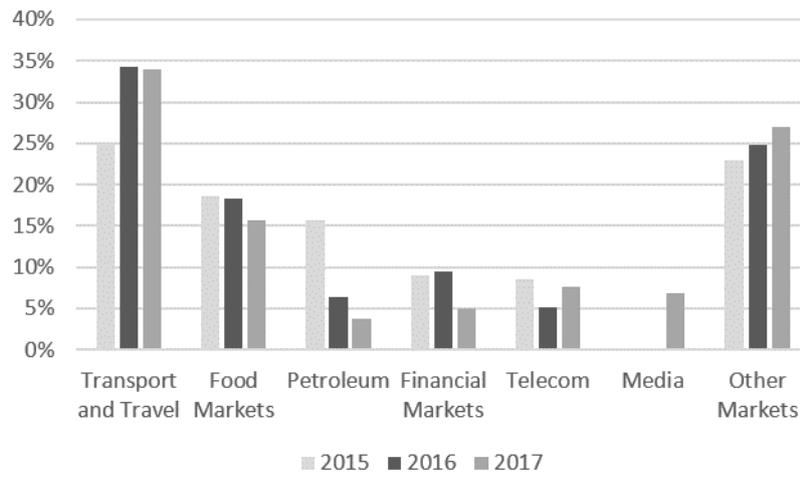
30. The ICA keeps track of and manages the allocation of employee’s work as regards various areas of responsibilities. The breakdown is based on time measurement.

31. Figure 2 shows clearly the shift to mergers in terms of allocation of time, as described in chapter 3.1.1. This affects the resources available for other work. Most notably, the ICA has had to reduce its emphasis on abuse cases which have traditionally been high on the agenda due to the oligopolistic nature of markets in many areas.

Figure 2. Allocation of resources - types of work



32. As shown in Figure 3, the ICA’s focus very much remains on transport and food markets.

Figure 3. Allocation of resources - markets

33. At the end of the year 2017, 24 employees were working at the ICA.