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The Qualified Zones in Transition: Navigating the Dynamics of the Euro-Israeli Customs Dispute

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I Introduction: The Issue Under Dispute

The principle of 'Rules of Origin' is a main motif in trade agreements. Determining the product's country of origin constitutes an assessment according to which it will be decided whether an infrastructure of various customs benefits will be accorded to the product. The issue of rules of origin is one of the main characteristics in the Association Agreement between the State of Israel and the European Union of 1995 (hereinafter the AA), and in light of recent developments, one of the claims is being scrutinized anew. The fourth protocol to the AA regulates and stipulates rules regarding origin of products. The rules also determine a 'verification' mechanism of the origin certificates, which serve as a reference according to which the product complies with the origin requirements.

In accordance with this mechanism and the awakening regarding violations of the rules of origin, applications have been submitted to the Israeli customs authorities by customs authorities of some of the EU Member States to verify the origin certificates on goods that the State of Israel exports to the EU and that originate in the Jewish settlements of the West Bank, Gaza Strip, East Jerusalem and the Golan Heights (hereinafter the Disputed Territories).

The origin certificates indicate the goods' country of origin as Israel. Following this, and further to the interpretation by the State of Israel of the trade agreement of 1975, which was signed between Israel and the EEC, and of the AA, trade with the Disputed Territories is entitled to preferential treatment like the other internationally recognized areas of the State of Israel, and therefore the AA incidence cannot be restricted on these territories. In contrast to Israel's stance, the EU insists on its claim, according to which

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these territories are not entitled to enjoy preferential treatment and the benefits bestowed on Israeli products (hereinafter the dispute). This spirit was stressed recently in October 2002 in a unilateral declaration diffused after the meeting of the EU/Israel Association Council, in which the EU restated the:

> great importance we attach to the correct application of the Association Agreement, in particular the territorial scope of the agreement … if the Association Council cannot find a solution, the EU will review its position in accordance with the provisions of the Association Agreement.[1]

Though the EU agreed in the October 2002 EU/Israel Association Council to extend the deadline with regard to customs on Israeli exports from the disputed territories until the beginning of 2003, in the meantime, European importers wishing to bring such articles into the EU will have to continue depositing money to cover the taxes should they eventually be imposed, and the Commision may very soon call on national customs administrations to transform into customs duties the importers' guarantees since November 2001 on products of doubtful origin, in accordance with the the EU 'Notice to Importers' of 23 November 2001 and the July 2001 concluding statement of the discussions of the committee for cooperation in customs matters between the EU and Israel.

During the October 2002 EU/Israel Association Council, the Israeli Foreign Minister Shimon Peres declared that the 'question is of minimal economic importance but of great political importance',[2] thus the dispute before us has become entirely political. From what arises and is discerned in the bilateral agreements which the State of Israel signed with the EU, there is no doubt that still at the beginning of the various trade obligations between Israel and the EU, the question of international sovereignty and responsibility that Israel has over the Disputed Territories was not raised. From a review of the agreements which were signed, it appears that the issue was not raised intentionally, and that according to international law and the GATT Treaty, Israel has territorial-international responsibility over these territories. However, this assumption should not mislead the reader. The saga over the valid interpretation of the AA with regards rules of origin and the applicability of these rules to products originating in the Diputed Territories, is by all means a difficult nut to crack. It appears from this that the nature of the issue before us creates the need to formulate a solution which will be based, apart from legal aspects, also on political and social principles recognized by the EU.

[1] See 'EU/Israel: EU and Israel Give Themselves till early 2003 to Find a Solution on Rules of Origin – Shimon Peres States Determination to Find Technical Solution to this Political Problem', *Buletin Quotidien Europe*, 8323, 10, 21–22 October 2002.

[2] Ibid.

1. The EU 'Notice to Importers' of 23 November 2001

At the end of November 2001 a Notice to Importers regarding the customs benefits accorded to goods produced in the Disputed Territories was publicized in the Official Journal of the EU. The Notice was preceded by bilateral meetings between Israeli and European delegations, in order to try and settle the dispute. The meetings discussed customs/technical aspects of the Dispute. In light of the EU desire to serve as a key player in the political process in the Middle East, in light of the slowdown in the political process, and in light of the pressures exerted on the EU by the Palestinian Authority, as also by other Arab states, the nature of the Dispute transformed from an economic-legal one to a political-state one:

> As to the substantial errors in the application of the Agreements, operators are informed that arising from the results of the verifications procedures carried out, it is now confirmed that Israel issues proofs of origin for products coming from places brought under Israeli administration since 1967, which, according to the Community, are not entitled to benefit from the preferential treatment under the Agreements.
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> Community operators presenting documentary evidence of origin with a view to securing preferential treatment for products originating from Israeli settlements in the West Bank, Gaza Strip, East Jerusalem and the Golan Heights, are informed that they must take all necessary precautions and that putting the goods in free circulation may give rise to a customs debt.[3]

The core solution proposed in this study is the recognition of 'Qualified Zones in Transition' (hereinafter QZT) as a solution for the dispute regarding the rules of origin and issuing Israeli origin certificates. Simultaneously with this solution, two additional alternatives will be proposed. The goal is to present possible solutions to the dispute with the EU regarding interpretation of the subject of rules of origin, and their analysis in view of the customary practice in the EU. The guiding principle is the combination of both legal and technical-based customs aspects and political aspects of the dispute, understanding the background and decision content and building a concept, interspersed with these aspects for settling the dispute.

[3] See Notice to Importers, 'Imports from Israel into the Community', *Official Journal of the European Communities*, 2001/C 328/04, 23 November 2001.

2. Article Structure

Following on from this introduction, Section II – The 'Qualified Zones in Transition' (the QZT) Mechanism – presents and analyses the core alternative proposed in our study for the dispute between Israel and the EU concerning rules of origin. This section also discusses how the QZT is to be implemented and guides our discussion in subsequent sections. Section III – Recognition of the Association Agreement Signed Between the EU and the PLO – presents and evaluates an additional alternative to the dispute.

This study is of the opinion that the dispute has the capacity to be referred to the European Court of Justice. This is the aim of Section IV. This section examines and criticises such a possibility, and debates its inherent problems. Section V highlights some of the important considerations that dominate the dispute before us and concludes our discussion.

II The 'Qualified Zones in Transition' (the QZT) Mechanism

1. Infrastructure

The State of Israel enjoys a unique status in the EU. The free trade agreement between Israel and the EU, which was upgraded to an Association Agreement, opens a wide window for cooperation. Israel is the only member that is not a Union country in several prestigious plans, such as the framework plan for R&D, and is slated, like all the Mediterranean countries, to be part of the free trade zone with the EU by the year 2010 (Barcelona Process). Further, an attempt is currently to integrate the State of Israel into the pan-European cumulation mechanism even before the year 2010. One of the most important facts in the discussion before us is the EU's status as the most extensive trade partner of Israel. However, the status of Israel is not free of problems inherent to a region which is influenced constantly by security problems that cloud the political situation. Despite these problems, the EU has expressed many times the importance that it attributes to the Middle East and the success of the political process. For example, the European Council decided as such in July 2000:

1. The Mediterranean region is of strategic importance to the EU. A prosperous, democratic, stable and secure region, with an open perspective towards Europe, is in the best interests of the EU and Europe as a whole.
2. The Mediterranean region continues to be faced with political, economic, judicial, ecological and social challenges. If these complex and diverse challenges are to be overcome, the EU and the Mediterranean partners must work together with a common vision, sensitivity and mutual respect.

5. The EU is convinced that the successful conclusion of the Middle East Peace Process on all its tracks, and the resolution of other conflicts in the region, are important prerequisites for peace and stability in the Mediterranean.[4]

Declarations of such type position the political process in the Middle East in the center of the activities and the strategy of the EU in all matters pertaining to the region. The alternatives for the solution of the rules of origin dispute proposed to the EU were reduced to the technical level. In our method, possibilities for solving the dispute cannot remain merely the fortification of customs or legal aspects. Therefore, the alternatives which will be proposed below combine, in parallel to the legal aspects, the political essence of the dispute.

2. Interpretations Enshrined in EU–Israel Agreements to the 'Recognised Area of Israel'

In order to examine the character and to appraise the essence of the dispute regarding the rules of origin, that mainly centers on the question, what is the effective-recognized area of Israel, and in order to construct an appropriate solution to the dispute, we will first discuss and review the interpretation given to this matter in the various agreements signed between Israel and the European Community.

Many questions arise from the phrasing of various paragraphs in the agreements. The answer to them is not clear, and disagreement regarding them deepens the dispute and turns it into one that is indubitably political in nature. The assumption at the base of the QZT mechanism hinges on the disagreement regarding the interpretation of 'the area of the State of Israel'. The term proposed below derives from the areas beyond the Green Line being the rock of dispute and the central element in the political dialogue, regarding which there is unanimity that their future is not clear. Therefore, we will relate to these areas as 'Zones in Dispute', or alternatively, 'Transitional Zones'. We emphasize that the term 'transition' should not mislead the reader, and that the meaning is not that these areas are being transferred to one side or another, but that are in an unclear space. As will be discussed below, the term 'transition' exists in EU jargon, and hence its appeal and its ability to constitute the beginning of an agreed solution.

[4] 2000/458/CFSP: Common Strategy of the European Council of 19 June 2000 on the Mediterranean Region, *Official Journal of the European Communities* 183, 22/07/2000, pp. 5–11.

Arguably, there is a valid assumption according to which the area of Israel includes the Disputed Territories has become customary over the years, since there was no official protest from the EU on this subject. This assumption is also based on the manner in which the various trade agreements between Israel and the EU are conducted, from which one can learn that 'the area of the State of Israel' includes the Disputed Territories. We will not examine the entire spectrum of legal foundations to this claim, but we will emphasize those that are relevant to the discussion before us. The analysis should begin with Article 31 to the Vienna Convention on the Law of Treaties of 1969 that lays down the fundamental rules of interpretation and can be taken as reflecting customary international law. Article 31(1) declares that a treaty shall be interpreted 'in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose'.[5] This is applicable regarding any document connected to the treaty, and regarding the custom created in this matter as said. The spirit that was customary between the EU and Israel reinforces the claim that the Disputed Territories are an inseparable part of the recognized territory of Israel.

Section 83 to the AA, Part IX regarding institutional, general and final instructions, stipulates in this phrasing:

> The Agreement shall apply, on the one hand, to the territories in which the Treaties establishing the European Community and the European Coal and Steel Community are applied and under the conditions laid down in those Treaties and, on the other hand, *to the territory of the State of Israel*.

In this matter it is fitting that we add the instructions of Article 29 to the Vienna Convention according to which:

> Unless a different intention appears from the Treaty or is otherwise established, a Treaty is binding upon each party in respect of its entire *territory*.

The question obviously is, what is the 'entire territory' of the State of Israel. A further source that is important regarding the answer to this question is the GATT Agreement. Article 26 (a) to the Agreement stipulates that:

> Each Government accepting this Agreement does so *in respect of its metropolitan territory and the other territories for which it has international responsibility*, except such separate custom territories as shall notify to the Executive Secretary to the Contracting Parties at the time of its own acceptance

[5] See for example the *German External Debts arbitration*, 19 ILM, 1980, pp. 1357, 1377.

In the same matter, a report of the International Law Committee of the UN (the ILC) determined that it refers to territory over which the countries that are members in a given agreement have 'international responsibility'.[6] Therefore, the claimant will claim that this rule should apply also to the Disputed Territories, as the State of Israel has international responsibility over these territories. Given that we are discussing the parties' intentions in interpreting the recognized area of Israel in relation to the rules of origin, we will seek the answer in the various trade agreements signed between the parties and relating to this matter.

The first trade agreement between Israel and the Europeans was signed in 1964. This agreement is limited in scope and the incidence paragraph does not appear. The second trade agreement was signed in 1970. According to this agreement, the State of Israel was accorded the status of MFN. According to the incidence paragraph of this agreement, (a) the agreement will apply on the one side to the European territories to which the agreement establishing the European Economic Community applies, and on the other side to the State of Israel, and (b) the agreement will apply to the French regions which are overseas. Hence, we can conclude that territories to which the agreement does not apply were restricted. Therefore, non-restriction of the Disputed Territories can testify to the fact that the parties' intention was that the recognized area of Israel includes also the Disputed Territories. Here Israel has 'international responsibility' over these territories. And if this is correct, then in our matter, the 'entire territory' should include also the Disputed Territories. Is this so? This is the place to repeat and emphasize that the parties' intentions regarding the interpretation of the recognized area of Israel should be seen as running on the political time axis. Such a distinction will testify that this dispute is political in essence.

In 1975 a comprehensive FTA agreement was signed with the European Economic Community in which it was determined that the agreement will apply on the one side to the territories to which the agreement establishing the European Economic Community applies, and under the terms determined in this agreement, and on the other side, to the State of Israel. In 1986, Regulation 9869/86 was adopted by the Council of Ministers of the EC regarding the import of goods originating in the West Bank and Gaza, without any restriction. Section 1 of the Regulation reads:

> Products other than those listed in Annex II to the treaty establishing the European Economic Community originating in the Occupied Territories shall be imported into the Community without quantitative restrictions or measures having equivalent effect and free of customs duties and charges having equivalent effect.

[6] Third Report, 1964 IL 15 YBILC.

Section 3 to the Regulation determines a mechanism with regard to rules of origin. We can define this Regulation as a turning point. The Council remarked that the FTA agreement of Israel with the EU does not apply to the Disputed Territories:

> Whereas no such preferential import conditions apply to products originating in the West Bank of the River Jordan or the Gaza Strip both occupied by Israel.

The Regulation of 1986, if so, is problematic regarding the interpretation of the recognized area of Israel. Despite the fact that even before passing the declaration and also after it, the export of goods manufactured in the Disputed Territories existed in force, the regulation constitutes a clear declaration of the EU regarding its understanding of the Disputed Territories. Still, we should bear in mind that this declaration is unilateral and it is not in its power to change the custom formulated according to the agreements.

Almost a decade subsequently, in 1994, the Paris Protocol was signed between Israel and the Palestinian Authority which defines their authorities. The Paris Protocol was attached as an appendix to the Interim Agreement which was signed between Israel and the Palestinians on 28 September 1995. The Interim Agreement was signed by the EU as a witness. The fact that the EU signed as a witness reinforces the claim that in terms of the interpretation, the EU, in the agreements it signed with Israel, was aware that the Disputed Territories constitute a part of the recognized area of Israel. This even reinforces the distinction that a change in the policies of the Europeans moves on the axis of the 'Policy Developments'. It is important to note that paragraph XVII (2) to the Interim Agreement stipulates that from a territorial aspect, Israel has the authority, among others, over the settlements – a subject which was agreed would be discussed within the framework of the permanent agreement. About two months after the EU signed the Interim Agreement as a witness, the FTA agreement was signed between Israel and the EU. The proximity between the two 'events' raises many questions regarding the EU's intentions as to the question of the recognized area of Israel. Here the EU signed the Interim Agreement as a witness, and according to it the authority over the settlements rests with Israel and, we continue, the EU does not restrict the Disputed Territories from the provisions of Section 83. To what extent restriction as said is required to limit the agreement's incidence can be learnt from the provision of Sections 36 and 37 of Protocol IV to the AA regarding the definition of the term 'Products of Origin'. For example, Section 36 determines that the use of the term Community in this protocol does not encompass Ceuta and Melilla,[7] and the term 'products originating in

[7] The regions of Ceuta and Melilla are governed by Spain but geographically are in Morroco.

the Community' does not encompass products that originate in these regions. Further, Section 36(2) declares that this protocol will apply to the products that originate in Ceuta and Melilla, with the required changes, subject to the special terms stipulated in Section 37.[8]

One can conclude and say that on the political time axis we can observe a change in the EU's stance regarding the way they perceive the Disputed Territories. On the other hand of course one can claim that the witting continuation of exports of goods manufactured in the Disputed Territories to EU Member States, with the EU having signed as a witness to the Interim Agreement, raises many questions. There is no doubt that the intensive activity of the EU in the Palestinian niche awakened the dispute and brought about the change in the its stance.

3. The QZT Mechanism

a) The base assumption. The QZT principle is based on the EU practice, according to which there are 'interim'/ 'in transition' situations. We request to make use of this practice regarding the issue of the rules of origin, that is, we propose a mechanism according to which the Disputed Territories will enjoy the status of 'interim/in transition situations'. In order to create terminological compatibility, we coined the definition 'Qualified Zones in Dispute'. The law of dispute is like the law of a particular situation being affected by lack of clarity, and accordingly, in an interim situation. The goal is to enable continuation of customs benefits to the Disputed Territories. The QZT mechanism assimilates the dispute regarding the interpretation of the recognized area of Israel on which we expanded above. Thus we are aware of the political nature of the dispute, and hence separating these aspects from the dispute is in a sense not finding a solution agreed to by the parties.

The QZT mechanism has two operational paths; independent and conditional. The preferred operational path is attuned to the spirit surrounding the issue of the rules of origin, a spirit that was expressed recently at the meeting of the Association Committee in Brussels, according to which the EU does not recognize the Disputed Territories as the area of the State of Israel, and therefore, the customs benefits do not apply to it, according to protocol IV to the agreement. At the center of the QZT is the subject of transition of which extensive use was made in the European legislation. Therefore, it is fitting that we start with examples that give support for the use of the proposed mechanism.

[8] The same distinction and limitation of Ceuta and Melilla regions from the agreement incidence exists also in paragraph 35 to protocol III in the FTA Agreement of the EU with the P.L.O. signed in 1997.

b) Examples of situations in 'transition'. A major example of a 'situation in transition' is the FTA agreement signed between the EU and the PLO (in favour of the PA). In this agreement the EU uses the term 'Transition'. It means there are interim situations. The method of 'Qualified Zones in Dispute' is based accurately on the same principle of 'interim situation'. The use that the EU makes of it in the FTA agreement with the Palestinians proves beyond all doubt that we can develop the concept of 'Situation in Transition'/ 'Qualified Zone in Dispute', and to implement it in the matter of the rules of origin. Section I(3) to the agreement, in the matter of the free movement of goods, stipulates in this phrasing:

> The Community and the Palestinian Authority shall establish progressively a free trade area over a *transitional period*, not extending beyond 31 December 2001, according to the modalities set out in this Title and in conformity with the provisions of the General Agreement on Tariffs and Trade of 1994 and of the other multilateral agreements on trade in goods annexed to the agreement establishing the World Trade Organization (WTO), hereinafter referred to as the GATT.

And paragraph 8(3) stipulates:

> In the event of serious difficulties for a given product, the schedule referred to in paragraph 2 may be reviewed by the Joint Committee by common accord, on the understanding that it may not be suspended beyond the maximum *transitional period of five years*. If the Joint Committee has not taken a decision within 30 days of its application to review the schedule, the Palestinian Authority may suspend the schedule provisionally for a period which may not exceed one year.

Therefore, the requirement of 'transitional period' does not exist in a vacuum; it exists in a conceptual and operative sense in the trade-agreement practice of the EU, and as such, testifies to the possibility of its implementation also in our matter.

An addition example is Regulation 2820/98 on the Generalized System of Preferences (known as the GSP Regulation) that relates to the term 'in transition'. Section 6 to the Preamble to the Regulation (a) depicts the importance of the Regulation to the third world countries; and (b) determines that also the customs benefits given according to the Regulation move on the time axis – which indeed is not defined accurately, and their interest is commercial. The paragraph stipulates:

> Whereas the Community scheme of generalized preferences should therefore continue in its development-oriented approach, focusing in priority on the countries which have most need of it, i.e., the poorest countries whereas

> the scheme should be complementary to World Trade Organisation (WTO) instruments and should foster the integration of developing countries into the world economy and the multilateral trading system; whereas the giving of preferences should accordingly be seen as a *transitional measure, to be used as needed and phased out when the need is considered no longer to exist*.

To conclude, it should be indicated that even though the GSP example is directed to countries considered as 'Third World Countries', this can demonstrate the vitality of the 'transition situations'. The transition territory can be defined as 'territory in dispute' to forestall the conclusion that Israel does not see the Disputed Territories as part of its area. Moreover, in order to comply with the political sensitivity of the subject before us, we add that the Annex to the GSP Regulation lists the entities and countries that can enjoy the Regulation. The Palestinian Authority is not listed in this Annex. There is room to examine whether the addition of the Palestinian Authority to the GSP Regulation is worthwhile to the Authority, and whether it can upgrade the spectrum of economic benefits given to it by the EU.

c) Application: two operational streams

(i) Operational Stream I: the QZT as an independent mechanism Operational Stream I is the recognition of an independent QZT, which is not tied to particular conditions. This recognition, despite being conducted on a defined time frame, gives Israel the tools required for a possible solution of the dispute. The Disputed Territories will continue to enjoy the same status they have today. However, the problems inherent in an independent solution are obvious, as this mechanism requires, in other words, that the existing situation be made permanent. Therefore, there is no doubt that the EU will not give its consent.

(ii) Operational Stream II: the QZT as a conditional mechanism Operational Stream II is wrapped up in several conditions, where the conditions serve to comply with the obvious impetus to find a solution to the dispute, while we preserve the responsibility of Israel over the Disputed Territories. Primarily, the question is, should the two go together unless they intend to do so? According to existing precedents, it seems that the answer is yes. This requires us a detailed explanation.

Operational Stream II is based, among others things, on the cumulation principle without the consent of the Palestinian Authority. A mechanism of regular cumulation is not applicable in the current situation, since the Palestinian Authority objects to the cumulation principle. It is true that consent is required for the cumulation, but the mechanism of cumulation has been examined until now in parameters of conventional cumulation

against the Palestinian Authority. Operational Stream II presents a mechanism of cumulation against the Disputed Territories; in other words, cumulation between the parent entity – Israel – and the Disputed Territories. This stream 'borrows' foundation principles from the mechanism of the QIZ – Qualified Industrial Zone. This principle deserves further explanation.

The Qualified Industrial Zone (QIZ) Agreement between Israel, Jordan and the USA was signed at the Economic Conference in Qatar in November 1997 and came into effect in March 1998. This agreement determines qualified industrial zones in Jordan, in which joint ventures between Israel and Jordan, which comply with the agreement criteria, can enjoy customs-free access to the markets in the USA, subject to the Free Trade Agreement (FTA) between the USA and Israel. The status of the Qualified Industrial Zones is granted according to product. In order to receive approval, the product should be produced or manufactured in the QIZ, or should be a commercially innovative, or be a different item as a result of cultivation, production or manufacture in the QIZ. According to the original arrangements, 'an innovative or different commercial item' is such that is substantially different as a result of treatment in the QIZ and carries a brand, trait or a new use. The approval processes are managed by a joint committee of Israel and Jordan.[9]

In short, according to the QIZ agreement, in order to qualify goods which are produced in a particular zone Y, it is required to accumulate a particular per cent of production in zone Y in addition to the cumulation in other zones. Generally, according to the proposed Operational Stream II, a particular percentage of the product should be manufactured in the recognized areas of Israel prior to 1967 and another percent in the Disputed Territories. We will relate to this stream as a QZT for the purpose of combined-internal cumulation, since it is an cumulation between the area of Israel that 'is not under dispute' and the Disputed Territories. We emphasize, of course, the fact that recognition by Israel of the internal cumulation mechanism can ascend to a political statement. In order to mitigate the political effect of this declaration, it will further be proposed to recognize the FTA agreement between the EU and the PLO in conjunction with the recognition of the QZT.

[9] Here it is opportune to emphasize that the FTA agreement between Jordan and the USA as of 24 October 2000 grants Jordanian goods with a gradual exemption from customs in the American market, and facilitates the free tax export to Jordan. The time span is 2 to 10 years. This agreement will ultimately bring about the abolishment of the need for the QIZ arrangement. It will be able to abolish incentives to Jordanian entrepreneurs to hold partnerships with Israeli entrepreneurs in the QIZ, seeing that the Jordanians will enjoy exemption for export to the USA without needing the cooperation with Israeli entrepreneurs. However, the FTA agreement also benefits Israeli entrepreneurs who are interested in a cheap labour force. Moreover, these entrepreneurs will no longer be restricted only to the QIZ zones and Israeli inputs. There are those who claim that the FTA agreement discourages any joint industrial adventures of Israelis and Jordanians, as the Jordanian entrepreneurs have additional alternatives for partnerships.

As stated, Operational Stream II is based, as mentioned above, on the cumulation principle, but does not require Palestinian Authority permission. This operational stream applies various principles accepted in the QIZ mechanism – existing between Israel, Jordan and the USA – to the rules of origin. In this regard, we would like to indicate that according to the rules of origin of the QIZ arrangement, it is required that at least 35 per cent of the valued rate of the product will be added in the QIZ. In the FTA agreement with the EU at least 40 per cent is required. A simple assembly, combination, wrapping or dilution does not comply with the qualitative requirements of production or manufacture in the QIZ. In the QZT mechanism we should find the right equation. This equation should not be as harsh as the accepted cumulation terms in the QIZ. This means, the assembly or combination should comply with the qualitative requirement of production or manufacture in the OZT. The basis for this is the sensitivity of the dispute and the fact that the cumulation is between the parent state and the Disputed Territories, and not between it and another sovereign entity.

We will point out that at least 35 per cent of the value of the materials of which use is made, come from the QIZ or from the partners' sides: 11.7 per cent from the Jordanian producer, 8 per cent from Israel (7 per cent for hi-tech products) and the remaining part from the USA or the Palestinian Authority. According to the methods, the calculations are based only on direct costs. For our matter, in order to impart to the mechanism better operative interest, we propose that a significant dominant value be created in the Disputed Territories, when the 'contribution' of the parent area, Israel, will be far lower. It can be defined as 'backup support'. It is proposed to allow the completion value from Jordan, the Palestinian Authority (that at this stage will not respond to it) or – like the USA can 'participate' in 'building the value' in the QIZ, so the EU Member States can 'participate' in 'building the value' of the goods originating in the QZT. It is recommended in the initial stage not to create a distinction between various branches such as agriculture and hi-tech industry.

It is submitted that in the USA–Jordan FTA agreement, a difficult problem is posed regarding the requirement to accumulate added value of 35 per cent in Jordan. Jordanian industrialists complain that cumulation of this value is not applicable in many cases, and therefore, they approached the Jordanian Government entities with this requirement to examine together with the American Government the possibility of 'cumulation value participation' with countries that have similar FTA agreements with the USA (that is, Israel, Canada and Mexico). It seems that the intention of the Jordanian industrialists is to Israel. The *Jordan Times* reviewed this matter and in its report of 7 October 2001 it was written:

Industrialists have repeatedly complained of the 35 per cent value added

Conditions for products to qualify since they are sometimes unable to meet the rule.

They are demanding that the FTA allow for the accumulated rules of origin. Under this formula, raw materials originating in other countries with which US has an FTA would be considered as Jordanian value added.

Based on the Jordanian requirement from the US, it is possible to present before the EU similar claims, and to suggest cumulation between the Disputed Territories and other countries which have FTA agreements with the EU.

One of the direct conclusions from the QZT mechanism is that the industry in the Disputed Territories can be enlarged should it comply with the cumulation rules we proposed. However, there is no doubt that from the viewpoint of the EU, this 'by-product' will be considered as misuse of the QZT mechanism, lack of bona fides and a fundamental violation of the agreement. Therefore, it is important to recall that contrary to the QIZ mechanism, where the inherent advantage enhanced industrial cooperation, in the QZT areas there is no reference to this type of cooperation but only setting of a given situation.

d) Additional elements. One of the most important elements in the QZT mechanism is that it is conducted on a time axis – it is not a permanent solution. This is also expressed in Section 6(1) to the Preamble of the GSP Regulation. The arrangement serves only as a milestone from which it will be possible to build a system to facilitate customs benefits also for goods manufactured in the Disputed Territories, but in parallel it will require the continued action in other fields. Also the EU–PLO FTA agreement points out that the periods of transition are defined in time. It is important to indicate that one should avoid limiting the time of the 'transition period'. There is the possibility of defining a general time framework according to which, in accordance with the political progress, the dispute of the rules of origin will reach its solution. However, one can assume that the EU, based on its experience, will not require a defined short-term period.

An additional element is the EU sensitivity to the protection of human rights. A toughening of the EU's stance with regard to rules of origin will hurt exactly that which the Union is trying to strengthen – human rights by way of upgrading economic development and trade relations. Cancelling benefits to goods originating in the Disputed Territories is like a death-blow to some of the industries and to agriculture. The result is a direct blow to the income sources of the Disputed Territories residents, that is, damaging the fundamental human rights. It is right that the policy line of the Union can be such as to stipulate that Israel is responsible for the human rights violation of the citizens in the Disputed Territories, given that it is responsible for the settlement in these areas. However, it seems that the Union will not raise this claim, both in light of Israel's accepting the area as a 'Disputed Area', and in light of

the fact that cancelling the benefits will result in real damage to fundamental human rights.

4. Interim Summary

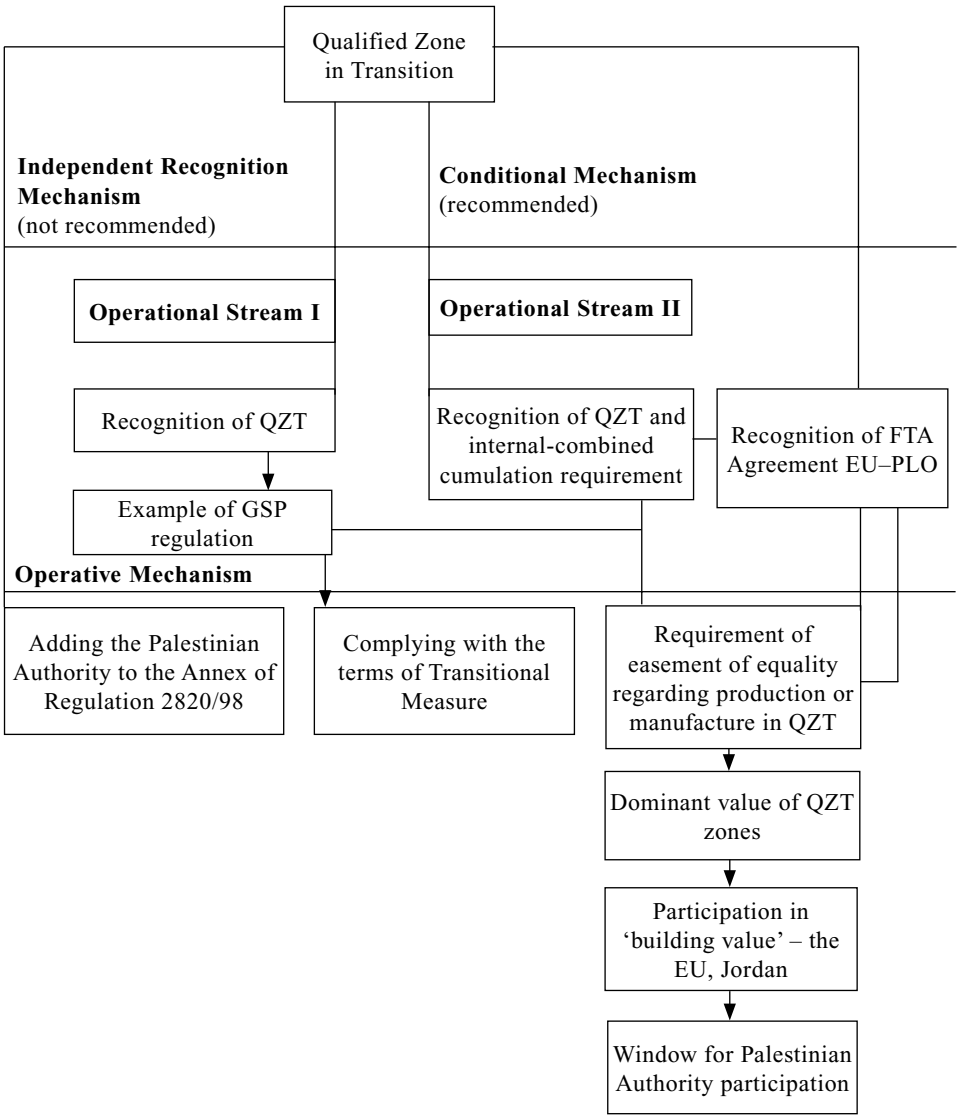
The key words 'temporary', 'human rights' and 'transition period' testify to the possibility of encompassing the same concept in the Disputed Territories. These terms may instil positive content in the issue, and may even serve faithfully the disputes that will arise following the recognition of the QZT zones. And in short, the required solution, and that which is proposed above, is fundamentally legal-political and is based on bilateral recognition of the QZT principle. The trilateral consent which includes the Palestinian Authority is indeed the end vision, but it does not appear that the Palestinian Authority will cooperate at this stage. In the agreement of the QZT matter, it can be indicated that the road is open for the Palestinian Authority to join the agreement. (See figure 1.)

III Recognition of the Association Agreement Signed Between the EU and the PLO

1. Infrastructure

We have already posited that the core of the dispute is political in nature. In light of this and in order to cast the political content for solving the dispute we propose to examine the recognition of the FTA agreement signed between the EU and the PLO as a possible alternative to the solution. The starting point is the contradiction that exists between the Interim Agreement between Israel and the Palestinian Authority, and the FTA agreement between the EU and the PLO. This is the reason why Israel does not recognize this agreement. Nevertheless, it is highly probable that the EU will reveal interest in this alternative, as apart from being on the political-readiness level on the side of the State of Israel, it certainly sides with the Palestinian Authority. Negotiations with the EU regarding recognition of this agreement, on the basis of trade-off, can prevent customs sanctions and continuation of discussion of the dispute. If that is the case, this alternative may serve the need to find an overall solution, and it may constitute a milestone in order to continue and discuss possible solutions, while blocking the imposition of customs on products from the Disputed Territories.

Figure 1. The QZT mechanism: concluding structure



Common Central Characteristics		
Palestinian Authority consent is not required	Temporary	Preserving human rights
Effect/Result		
A mechanism for solving the dispute		Continuation of customs benefits/setting a given situation

2. The Contradiction between the Interim Agreement and the EU–PLO FTA Agreement

Israel sees the Interim Agreement, in which the Paris Protocol is included as an Appendix, as an agreement in effect. As such, the AA between the EU and the PLO, which was signed on 24 February 1997, stands in contradiction to the Interim Agreement, since it creates new and broad authorizations for the Palestinians, authorizations that the Interim Agreement explicitly does not grant. The incidence paragraph stipulates:

> This Agreement shall apply, on the one part, to the territories in which the Treaty establishing the European Community is applied and under the conditions laid down in the Treaty and, on the other part, to the territory of the West Bank and the Gaza Strip.

The EU sees the West Bank and Gaza region as a uniform territorial region. This conclusion can be based also on the phrasing of Section 5 according to which:

> No new customs on imports, or any other charge having equivalent effect, shall be introduced on trade between the Community and the West Bank and Gaza Strip.

We further add that Section 15(1)(a) to Protocol III to the EU–PLO AA regarding the 'Origin Products' stipulates that EUR 1 certificates, similar to how business is conducted with Israel, will be issued accordingly. The Protocol uses the words: 'A movement certificate EUR 1 shall be issued by the customs authorities of the exporting country….' Hence, the way is paved to ask: Does the EU relate to the Palestinian Authority as a state? It is possible that the answer is yes. However, we should bear in mind that first and foremost, the PLO, the entity which signed the agreement in favor of the Palestinian Authority, does not represent a state and does not have the authorization to sign an agreement, as stated, on behalf of a state. Secondly, a signature on the AA constitutes a violation of the Interim Agreement provisions. It is interesting to note that if the EU provides explicitly that it sees the West Bank and Gaza Strip as one bloc, which enjoys customs benefits, why limit the incidence to the Disputed Territories? The Union itself creates an anomaly in the agreement: on one side, the region is one unit; on the other side, the region is divided according to patterns of sovereignty to which it does not agree. One way or the other, the EU leaves the readers with one conclusion that can be reached in two ways:

(a) If the region is one bloc which enjoys customs benefits, it includes also the Disputed Territories, and

(b) If the region is not one bloc, then the Disputed Territories are a part of the recognized area of Israel, and therefore are in a district which enjoys customs benefits according to the AA between the EU and the State of Israel.

From the paragraph language quoted above we can learn that the EU wants to see the Palestinian Authority as a state with broad authorization over all the West Bank and Gaza Strip territories. The agreement creates contradictory authorizations to the Interim Agreement, as it defines authorizations that deviate from those granted to the Palestinians according to the Interim Agreement. It is stressed again that the EU signed the Interim Agreement as a witness, and the question of lack of bona fides arises here in all its glory.

3. Additional Terms for Recognition

In spite of the contradiction between the EU–PLO AA and the Interim Agreement, it is proposed that Israel consider recognizing the former. Of course, the first condition accompanying the step as said, is the recognition of the QZT areas. In parallel, it is proposed that also an upgrading of the cumulation mechanisms of Israel be adjoined to this condition. It is true that Israel enjoys a unique status in the EU, but it would be fitting that the cumulation subject be reopened for discussion. We relate mainly to the Pan-European cumulation mechanism. This cumulation mechanism is a relatively new arrangement. According to Priess, this mechanism is in the sense of 'the beginning of a new era',[10] a quasi-harmonization of the rules of origin: determination of uniform rules of origin in the 'Enlarged European Trade Zone'. This will allow several countries to be considered as one country in the matter of rules of origin.[11] In other words, the product input can be taken from several different sources, and in terms of the rules of origin, the product will be considered as created in one country. The mechanism applies to fifteen Member States of the EU, the European Economic Area countries, Switzerland, East and Central European countries and the Baltic countries.

The inclusion of Mediterranean partners of the Euro-Mediterranean Partnership in the pan-European cumulation system was considered in many occasions, and recently the Valencia Fifth Euro-Mediterranean Conference of Ministers for Foreign Affairs decided:

[10] H. Priess and R. Pothke, 'The Pan-European Rules of Origin: The Beginning of a New Era in European Free Trade' (1997) 34 *Common Market Law Review*, pp. 773–809.

[11] See, in depth, M. Hirsh, 'The Pan-European Rules of Origin and the State of Israel' *The Israeli Tax Law Quarterly*, Kaf-Tet (114) 42–53 (in Hebrew).

to accept the principle of the participation of the Mediterranean partners to the system of pan-European cumulation of origin and urged:

a) The Continuation of the technical work of the working group on rules of origin to solve practical problems and to reach concrete proposals at the earliest.
b) The introduction of the necessary amendments to the Association Agreements' protocols.
c) The conclusion of Free Trade Agreements with harmonised rules of origin between the Mediterranean partners.[12]

The Inclusion of the Mediterranean countries in the pan-European cumulation system is likely to take several years. This study is of the opinion that an element to the willingness of Israel to recognize the AA signed between the EU and the PLO may be a fast-track procedure that would enable Israel to be included in the pan-European rules of origin machinery.

The exclusion of Israel from the pan-European cumulation mechanism places Israel in an inferior position against European countries regarding the commercial contest.[13] Again, the most important and influential fact is Europe being the largest trade partner of Israel. Israel is permitted to collect inputs only from its area (and following the 'Notice to Importers' of 23 November 2001, the Disputed Territories are not included[14]), apart from the exception of the tolerance rule that stipulates that 10 per cent input of a particular product can be collected from other origins (except for textile and clothing products). In contrast with Israel, the European competitor can collect product inputs from all the countries participating in the Pan-European arrangement, can reduce costs, enjoy zero customs and a pure economic advantage over other countries. For example, Section 3 to the Protocol of the EU agreement with the Czech Republic stipulates that:

Materials originating in the Community shall be considered as materials originating in the Czech Republic when incorporated into a product obtained there (and vice versa) … It shall not be necessary that such

[12] Fifth Euro-Mediterranean Conference of Ministers for Foreign Affairs, '*Valencia Action Plan*' (EMP Valencia 23/04/2002) 5, Point 6

[13] An example from the flower sector testifies to the blow to competition. In principle, Israel is a member in the trade liberalization process of agriculture produce in the EU. This increases the Israeli breeder's exposure to competition within Israel, and simultaneously opens to them more markets and opportunities in Europe – seemingly a type of summetry. However, in force, several European countries are not ready to stop using the mechanism of relative costing in the flower sector – and not only towards Israeli exports. This mechanism is destructive for the rose breeders in Israel, because the exporters do not know if they will enjoy preferential customs until their cultivars reach the EU.

[14] As discussed above.

> materials have undergone sufficient working or processing, provided they have undergone working or processing going beyond insufficient working to confer origin.

Should Israel be allowed to be a member in the same 'countries club' that enjoy the Pan-European arrangement, products produced in Israel and in other groups of non-European countries, such as Egypt and Jordan, could enjoy the ability of 'origin cumulation' and fairer competition. Apart from upgrading the cumulation possibilities, a very welcome by-product is likely to emerge; regional cooperation.

4. Interim Summary

The slowdown in the political process brought the EU to raise the inherent, though silent, dispute to the AA. The dispute, the solution to which was expected to be found in legal or customs-technical frameworks, became political. This dispute did not arise in the previous stages of bilateral-commercial obligations between Israel and the EU, however, its face changed in accordance with the political processes in the Middle East. The dominant spirit in the EU was expressed at a meeting of the Association Committee which convened in Brussels on 21 May 2001 with the participation of executive officials of the EU Commission and Israel:

> The EU is concerned about the continuing Israeli settlement activities. Settlements are illegal under international law and constitute a major obstacle to peace, and the EU is concerned about the plans to establish new settlements as well as the plans to expand already existing ones. The EU strongly urges the Israeli government to reverse its settlement policy as regards the Occupied Territories, including East Jerusalem, and to put an immediate end to all settlement activities.

This declaration explains the politicization of the dispute revolving around rules of origin. There is place for the claim of lack of bona fides on the EU side, in light of the fact that it signed the Interim Agreement as a witness. Moreover, there is no doubt that the AA between the EU and the PLO contradicts the Interim Agreement, which limits the authorizations of the Palestinian Authority.

The recognition of the FTA Agreement between the EU and the PLO should be regarded as an opening for the recognition of QZT areas. In our opinion, Israel and the EU profit from recognizing such QZT areas. Arguably, recognizing the FTA Agreement does not bear much significance for the EU, since in terms of the daily conduct, the FTA Agreement between the EU and the PLO was signed, and according to its provisions thus is the situation in

practice. Therefore, does the 'yes' of Israel have any substance? It appears not. However, a declaration from Israel that it recognizes the Disputed Territories as disputed zones serves the Israeli interest, that these territories will constitute a recognized territory of Israel, and a product manufactured in these territories will continue to enjoy customs benefits, and at the same time – in a declaration, as said – there is a response to the political desire of the EU to be involved in the Middle East peace process. One should not forget that such a statement by the Israeli government should be welcomed by the EU, as Israel takes upon itself that the Disputed Territories are a main part of the Israeli-Palestinian dialogue, that their future is in dispute, and that they do not form a recognized part of the State of Israel.

IV Referring the Dispute to the Interpretation of the European Court of Justice

1. Characteristics

Referring the dispute to the European Court of Justice (ECJ) for interpretation, is an additional alternative at our disposal. Although it is beyond the scope of the present study to provide a thorough analysis of the possibilities of filing a suit within the ECJ, it is of vital importance to provide the reader with the most viable possibilities that might bring the dispute before us to Luxembourg.

There are several possibilities which can lead the dispute to discussion in the ECJ. For example, when European importers attack the demand for deposit in the court of their country of citizenship, the local courts will be required to decide on this dispute, whether these are territories of Israel that should enjoy custom benefit under the AA, or not. Such an issue was not judged previously in the European Court and there is no precedent in this matter. According to Article 234 of the EC Treaty, there is a duty to refer such matters, which was not discussed before, to the ECJ, in order to obtain the Court's instruction as to how to interpret the case. Israel has the right to intervene at the commencement of the proceedings, in other words, in the court of the member country, and to request, if the laws of this country so allow, to refer the issue to the ECJ's instruction. In the event that the case is referred to the ECJ, Israel has several possibilities of locus standi.

Article 232 of the Treaty concerns a declaration on the part of the ECJ or the CFI that the defendant institution acted unlawfully by failing to take a decision. Such a failure is unlawful only if the defendant institution was under a duty to act. Bearing Article 232 in mind, there is the possibility that an EU Member State or an institution will file a suit in the ECJ against the Commission for not enforcing the said rules regarding Israeli goods

manufactured in the Disputed Territories. In other words, the Commission has failed to take a decision. This possibility is not theoretical, particularly in light of the call by ministers in governments of Members States, as well as of MEPs, to put an end, in their words, to Israel's violation of rules enshrined in the Agreement between Israel and the EU. Today, following the Notice of the 23 November 2001, the ground is still ready for such claims to be developed, if the Notice is not implemented. At the same time, however, one should be attentive to the fact that the Commission or a Member State can bring an action for infringement of Community law by a Member State under the stipulations of Articles 226–228 of the EC Treaty.

The spectrum of legal claims that can be filed with the European Court is broad. Despite its scope, we should bear in mind that the court assembly is influenced by politics: political considerations are mixed up in the appointment of judges which in turn cloud the professionals' considerations. The possible legal claims include inter alia the interpretation of the sides' intentions in light of the agreements signed and their conduct; violation of the 'good faith' principle; 'estoppel'; and the legitimate expectations claim. The latter refers to the fact that, except for Israel, exporters and importers also relied on the AA and the customary practice created in the matter of fulfilling its provisions relating to rules of origin, and in our matter, providing customs benefits also for goods that originate in the Disputed Territories. Under these circumstances, the EU is likely to be found in violation of the principle of 'legitimate expectations'.

In spite of the above, it is important that we be attuned to several basic characteristics of the court and its assembly, which will raise questions regarding the necessity for the results of discussions in this forum. We emphasize that it is not our opinion to adopt this alternative at this stage as (a) filing an application with the ECJ certainly may cause additional diplomatic 'incidents', and (b) the rulings prove that the political paths of the Court are sometimes not hidden.

2. Analysis

The locus standi subject of countries that are not members of the EU, in the ECJ, was virtually not discussed in writing. The Court has two instances and both of them have criteria for locus standi. The dispute regarding the rules of origin is an example of an incident that may be discussed in the ECJ. Further to the above regarding the ways in which the dispute can be required for the ECJ's interpretation, we would like to set out the locus standi of Israel. In the following discssion we will examine three core possibilities of locus standi for non-member countries of the EU in the ECJ.

The first possibility is the action for annulment pursuant to Article 230 of the EC Treaty. This Article enables Community institutions, Member States, and natural and legal persons to protect themselves against unlawful binding acts of Community institutions (provided that specific conditions as to admissibility are fulfilled). Can Israel be regarded as a natural or legal person and hence rely on Article 230 in order to request the ECJ to annul the Commission's Notice to Importers? For this subject the Court was required in the case of *Chris International v. Commission*,[15] in which the ECJ was required to rule regarding the locus standi of the Dominican Republic before it against the resolution of the European Commission in the matter of protection of the local banana market in England. The European Court ruled that the Dominican Republic has the locus standi because it fulfills the requirements of Article 230, according to which:

> Any natural or legal person may, under the same conditions, institute proceedings against a decision addressed to that person or against a decision which, although in the form of a regulation or a decision addressed to another person, is of direct and individual concern to the former.

From this precedent[16] one can conclude that Israel, by virtue of Article 230, has two ways to plead before the Court: first, if a particular decision is directed directly to Israel, Israel has the right to apply to the ECJ. This means the decision publicized in November 2001 constitutes a reason to apply to the ECJ by Israel, as it is directed directly and influences in the same manner the State of Israel. And second, decisions which are not directed directly to Israel, but Israel is affected by them, also can create the locus standi.[17] For example, if the European Commission stipulates that a particular export does not fulfill the rules of origin criteria, or that a member country did not comply with these criteria, but the decision is not directed against Israel but to the same member country, there is no doubt that Israel is affected. Therefore, a similar case is in the sense of 'a decision addressed to another person, is of direct and individual concern to the former'.

The second possibility is intervention in proceedings according to Section 37 to the EC Statute of the Court of Justice. Section 37 stipulates that any person who has interest in the results of a case that was under discussion in

[15] Joined Cases 91 and 200/82 *Chris International Foods v. Commission* (1983) EUR 417.

[16] In this regard see also, case C-298/89 *Government of Gibraltar v. Council of the European Communities*, Special Edition (SSE) (1993) 0243. Judgement of the Court of 29 June 1993, ECR (1993) I-3605. See also K. Lenaerts and D. Arts, *Procedural Law of the European Union* (1999), Chapter 7, pp. 139–206.

[17] Case T-96/92 *CCE de le Societe des Grandas Sources v. Commission* (1995) ECR 11-1213,1236-1237, 45; Joined Cases C-68/94 and C-30/95 *France and SCPA and BMC v. Commission* (1998) ECR I 1375, 1470,51.

the Court, has the right to intervene in proceedings. In the *Chris International* judgement, the European Court ruled that a third country is a 'person' for the matter of Section 37 to the Statute (the EU institutions are not obliged to show interest). If so, Israel has the right to intervene in the proceedings of the Court should it show that it has interest in the trial results. For example, if the customs authorities of Denmark or Greece decide to file suit in the European Court pleading that other countries are not fulfilling the duty to require deposits or apply the criteria of the rules of origin, according to Section 37, Israel can intervene in the proceedings.

The third and perhaps the most viable and interesting possibility for locus standi of Israel in the ECJ is indirect use of Article 234, called by many 'Court leverage' as it is a legal tool which the member countries, institutions and citizens use extensively, and based on it, the Court issues many precedents. Thanks to this discussion tool the European Court has become one of the institutions that leads the EU integration process. Article 234 stipulates:

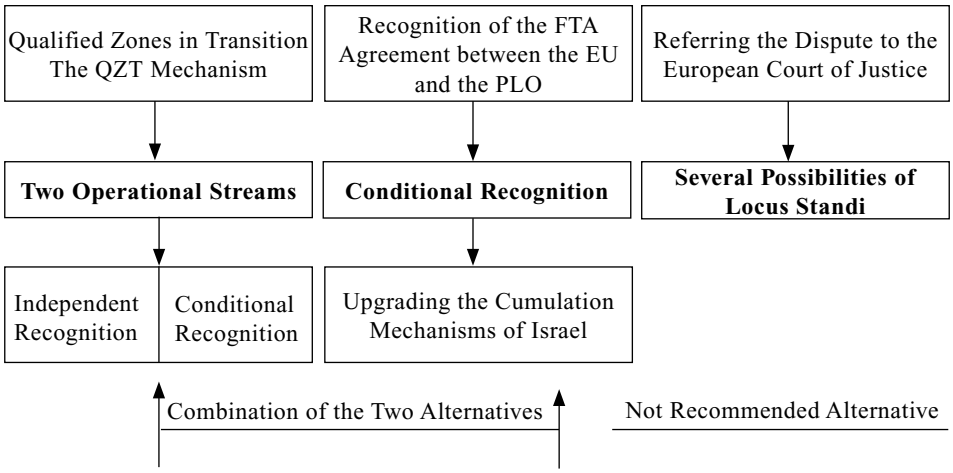
> The Court of Justice shall have jurisdiction to give preliminary rulings concerning:
> (a) the interpretation of this Treaty;
> (b) the validity and interpretation of acts of the institutions of the Community and of the ECB;
> (c) the interpretation of the statutes of bodies established by an act of the Council, where those statutes so provide.
>
> Where such a question is raised before any court of tribunal of a Member State, that court of tribunal may, if it considers that a decision on the question is necessary to enable it to give judgement request the court of Justice to give a ruling thereon …

To our matter, the use of Article 234 is problematic, since Israel cannot operate it indirectly. This means, if the dispute concerning the rules of origin arises before a Tribunal or a Court of one of the EU Member States, Israel, according to the law of that country in which the dispute is raised, may enjoy the locus standi, and thus influence the local court to refer the dispute to the ECJ. Israel cannot require referral as said, but can raise the possibility before the local court discussing the dispute.

V Conclusions

The Commission's 'Notice to Importers' of 23 November 2001, stipulates that the Disputed Territories are not part of the 'recognised area of the State of Israel' to which the Association Agreement applies, and therefore, goods which are exported to the Union countries, that originate in the Disputed

Figure 2. Concluding structure



Territories, cannot enjoy the customs benefits according to protocol IV of the agreement, which discusses the rules of origin matter. 'Upgrading' the rules of origin dispute from the customs-technical to the political level raises many questions. The main question that arises is whether the Association Agreement is a cascade of possibilities for additional political disputes in the future. The answer to this question might be 'yes', since in the case before us the EU found a sufficiently wide crevice to raise an unequivocal bilateral subject to the international level, with extensive political and economic implications.

There is a real need to seek and find a solution to the dispute, in particular in light of the effect the EU resolutions have on the industry and agriculture of the Disputed Territories. Israel is required to mediate between the political desire of the EU – which found its way in the decision regarding the rules of origin – and the need to prevent abolishment of customs benefits. The solution proposed above, that is, the QZT mechanism which is accompanied by an Israeli gesture to recognize the FTA Agreement signed between the EU and the PLO, may be the one on which to mediate in the dispute before us. The advantage in the mechanism proposed is that it is not sabre-rattling but comes to determine a given situation simultaneously with a declaration capable of paving the way for new regional acheivements.