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DAVID P. FIDLER

INTRODUCTION

The Israeli-Palestinian peace process has many complicated and controversial features, but perhaps none so complex and politically charged as the strategy for Palestinian economic development. The leaders who gave the peace process life believed that its success depended on the economic development of the West Bank and Gaza Strip (the "Palestinian Territories" or "Territories"). The Palestinian economic development strategy involves a number of important elements, but central to the entire strategy is the objective of creating conditions that allow Palestinians to engage in regional and global trade. Three years after the Rabin-Arafat handshake that objective remains illusive. Suicide bombings undertaken by the radical Palestinian group Hamas in Tel Aviv and Jerusalem in March, July, and September 1997 have sent the peace process into its darkest moments, prompting the direct interven-

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1. Keith C. Molkner, Legal and Structural Hurdles to Achieving Political Stability and Economic Development in the Palestinian Territories, 19 FORDHAM INT'L L. J. 1419, 1420 (1996) (noting that "real economic growth that is rapid, profound, and sustained" was a major criterion for successful implementation of Palestinian autonomy).

2. See infra note 5 and accompanying text.
tion of U.S. Secretary of State Madeleine Albright. The recent and deepest crisis in the peace process has also adversely affected economic development in the Palestinian Territories.

This Article examines the development of Palestinian trade law during the peace process and identifies the major obstacles to the creation of significant trade opportunities for the Palestinian people. Underlying my analysis is a fundamental tension in the peace process: without peace between Israel and the Palestinians, Palestinian trade will not develop adequately, but without adequate trade, Palestinian faith in the peace process will be eroded by the lack of economic opportunity. I propose an alternative way to structure the trade arrangement between Israel and the Palestinians that might offer a way to overcome the "no peace, no trade—no trade, no peace" dilemma that currently haunts the peace process.

I. THE PALESTINIAN ECONOMIC DEVELOPMENT STRATEGY AND THE IMPORTANCE OF TRADE

A. The Economic Development Strategy

The leaders who crafted the peace process believed "that Palestinians who see no improvement in their standard of living or find no economic opportunities as a result of the peace process will question the wisdom of making deals with Israel and perhaps support forces that oppose the peace process." 3 Odin Knudsen, the World Bank's former Resident Representative in its West Bank and Gaza Resident Mission, stressed the importance of Palestinian economic development to the peace process by arguing that, without an economically viable Palestinian entity, "the Palestinians will become more impoverished, breeding more resentment and hostility towards Israel." 4 This perspective explains why experts analyzing the current state of the Palestinian economy are worried about the prospects for the peace process.

The economic development strategy created for the Palestinian Territories contained four fundamental elements. First, Israel and other developed countries would provide substantial aid to help

the Palestinians build a modern economic infrastructure.\(^5\) Second, Israel and the Palestinian Territories would continue to have close economic relations to maintain continuity with the economic dynamics built up during the Israeli occupation. Third, the improved Palestinian economic infrastructure combined with potential market opportunities in Israel and the region would attract significant amounts of foreign private investment. Although the World Bank believed that aid would be needed, it recognized that the private sector, stimulated by foreign investment, would have to be the real engine of Palestinian economic development.\(^6\) Fourth, the private sector in the Palestinian Territories would need access to foreign markets in addition to those in Israel. Trade with other regional economies and with more distant markets was, thus, integral to the success of the Palestinian private sector and to attracting foreign investment.\(^7\) Creating opportunities for Palestinians to trade regionally and globally became a central feature of the Palestinian economic development strategy.

B. Challenges to the Economic Development Strategy

The obstacles to the creation of regional and global trade opportunities for Palestinians have been considerable. In 1993, the World Bank concluded that economic patterns in the Palestinian Territories since 1967 were conditioned by, among other things,

5. See INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT, 1 DEVELOPING THE OCCUPIED TERRITORIES: AN INVESTMENT IN PEACE, Overview 9 (1993) [hereinafter WORLD BANK, Overview] (identifying serious infrastructure problems in the West Bank and Gaza economies). The peace process has witnessed many problems with the flow of international aid from donor countries to the Palestinian Authority, which are beyond the scope of this article to discuss in detail. For an overview of the aid program to the Palestinian Authority, see Palestinian Dev. InfoNet, Development Assistance to the West Bank and Gaza: An Overview (last modified March, 1997) <http://www.arts.mcgill.ca/MEPP/PDIN/pdoverview.html>.

6. WORLD BANK, Overview, supra note 5, at 13, 15. As with the international aid program, the objective of increasing foreign investment in the Palestinian Territories has encountered many problems. For a detailed overview of the obstacles confronting this objective, see Fidler, supra note 3. The World Bank reported that private investment in the Palestinian economy fell “from $750 million (or 26 percent of GDP) in 1993, to $435 million (13 percent of GDP) in 1995.” World Bank, The West Bank and Gaza: Country Overview (visited Sept. 10, 1997) <http://www.worldbank.org/html/extdr/offrep/ mena/wb&g.htm>. Approximately 90% of this investment was domestic rather than foreign. Id.

7. The World Bank noted that anticipated access to markets in Israel, the rest of the Middle East, and Europe helped “give West Bank and Gaza appreciable economic potential.” World Bank, The West Bank and Gaza: Country Overview, supra note 6.
“asymmetric trade relations” with Israel and the rest of the world.

During the Israeli occupation, Palestinians conducted trade mainly with or through Israel both with respect to exports and imports. In the mid-1980's, the Palestinian Territories purchased 90% of their imports from Israel and sold 75% of their exports to Israel. Palestinian trade dependence on Israel did not result from Palestinian enterprises acting upon the principle of comparative advantage but from Israel’s military occupation and political control over the Palestinian Territories. Israeli goods flowed freely into the West Bank and Gaza, but Palestinian goods that competed with Israeli products were either banned or heavily limited from entering Israel. Commentators also noted the “devastating effect” the Arab boycott of Israel had on the Palestinian economy because it cut off exports of goods to the Arab world from Palestinian enterprises.

8. INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT, 2 DEVELOPING THE OCCUPIED TERRITORIES: AN INVESTMENT IN PEACE, The Economy, 45 (1993) [hereinafter WORLD BANK, The Economy]. The argument about the asymmetrical development of the Palestinian economy since 1967 is not to be confused with a claim that Israeli occupation produced no economic development. The World Bank reported that between 1968 and 1980, the Palestinian economy rapidly grew because of many factors, "including the rapid integration with Israel and the regional economic boom." WORLD BANK, Overview, supra note 5, at 4. This growth, however, took a certain form that has produced the structural imbalances now present in the Palestinian economy. For an historical analysis of the economies of the West Bank and Gaza since 1918, see Roger Owen, Economic Development in Mandatory Palestine: 1918-1948, in THE PALESTINIAN ECONOMY: STUDIES IN DEVELOPMENT UNDER PROLONGED OCCUPATION 13 (George T. Abed ed., 1988); Antoine Mansour, The West Bank Economy: 1948-1984, in id., at 71; and Ziad Abu-Amr, The Gaza Economy: 1948-1984, in id., at 101.

9. Samir Hazboun et al., The Economic Impact of the Israeli PLO Declaration of Principles on the West Bank, Gaza Strip and the Middle East Region, 3 ISRAEL/PALESTINE ISSUES IN CONFLICT—ISSUES FOR COOPERATION 2, 7 (1994) (noting that “[t]he bulk of Palestinian goods for the last 26 years has been traded mainly with neighboring Israel and to a lesser extent Jordan.”).

10. WORLD BANK, The Economy, supra note 8, at 45.

11. Hazboun, supra note 9, at 7. The principle of comparative advantage was summarized as follows in a report prepared for the General Agreements on Tariffs and Trade: Trade allows countries to concentrate on what they can do best. No two countries are exactly alike in natural resources, climate or work force. Those differences give each country a ‘comparative advantage’ over the others in some products. Trade translates the individual advantages of many countries into maximum productivity for all. This is the classic theory of international trade.


12. Hazboun, supra note 9, at 7.

13. Id. at 7-8. For a discussion of the Arab boycott of Israel, see INTERNATIONAL BANK FOR RECONSTRUCTION, 3 DEVELOPING THE OCCUPIED TERRITORIES: AN
The consequences of Palestinian trade dependence on Israel went beyond export and import statistics because this asymmetric relationship adversely affected how the Palestinian economy developed. Two very important adverse consequences were (1) the low industrialization in the Palestinian Territories produced by the lack of incentives to expand manufacturing, and (2) the excessive reliance on the export of labor to the Israeli market. The Israeli occupation left the Palestinian economy distorted in its economic infrastructure, reliant on the Israeli market for employment opportunities, and almost totally dependent on Israel for imports and exports. Creating more diversified trade opportunities for Palestinians within the context of a distorted economic structure would, given the best of conditions, prove immensely challenging.

The distorted nature of the Palestinian economy created during the period of occupation underscored how important each of the elements of the economy development strategy would be. Aid and foreign private investment would be needed to develop the economic infrastructure, promote the growth of manufacturing, and provide employment opportunities for the Palestinian labor force. Foreign investors would need access to the lucrative Israeli market as well as opportunities to use the West Bank and Gaza as export platforms to other regional and world markets. If any of the elements ran into difficulty in implementation, then the entire

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14. Hazboun, supra note 9, at 9 (discussing impact of trade asymmetry on Palestinian industrial development). See also GEORGE T. ABED, THE ECONOMIC VIABILITY OF A PALESTINIAN STATE 12 (1990) (arguing that during the occupation "Israel's administrative powers (such as its licensing authority) were used to suppress industrial development.").

15. WORLD BANK, The Economy, supra note 8, at 47 (noting that "the West Bank and Gaza exported labor in the place of goods, partly because of an asymmetric structure of incentives").

16. The World Bank enumerated the following structural imbalances in the Palestinian economy in 1993: "(i) heavy dependence on outside sources of employment in the OT [occupied territories] labor force; (ii) an unusually low degree of industrialization; (iii) a trade structure heavily dominated by trading links with Israel . . . ; and (iv) inadequacies in the provision of public infrastructure and services." WORLD BANK, Overview, supra note 5, at 5.

17. The World Bank emphasized this point in arguing that in Palestinian economic development "[m]uch will also depend upon the quality of economic management in the post-peace period and the strategic choices made in managing the OT economy." Id. at 13.
economic development strategy for the Palestinians would be jeopardized.

II. IMPLEMENTING A PALESTINIAN TRADE STRATEGY THROUGH THE OSLO ACCORDS

A. The Declaration of Principles

The Declaration of Principles on Interim Self-Government Arrangements ("Declaration of Principles")\(^\text{18}\) signed September 13, 1993 launched the peace process, and it recognized the importance of Palestinian economic development.\(^\text{19}\) Annex III of the Declaration of Principles commits Israel and the PLO to "[c]ooperation in the field of trade, including studies, and Trade Promotion Programs, which will encourage local, regional and inter-regional trade . . . ."\(^\text{20}\) Some predicted that the Declaration of Principles would affect Palestinian trade enormously.\(^\text{21}\) The Declaration of Principles did not, however, establish a blueprint for a Palestinian trade strategy.\(^\text{22}\) In fact, the Declaration of Principles papered over some tensions between the Palestinians and Israel on the form of the trade regime for the West Bank and Gaza.\(^\text{23}\)

B. The Economic Protocol

The fundamental document providing structure for a Palestinian trade strategy for the peace process has been the Protocol on Economic Relations between Israel and the PLO ("Economic Proto-


\(^\text{19}\) The Economist Intelligence Unit Ltd., *Economic Policy and Economy*, Economist Intelligence Unit Country Reports, Dec. 10, 1993, at 1, *available in* LEXIS, Mdeafr Library, Allmde File (noting that the Declaration's provisions on economic development and cooperation "indicate recognition by the two sides that the success of their peace deal depends in large part on bringing about an immediate tangible improvement in living standards for Palestinians . . . .").

\(^\text{20}\) Declaration of Principles, *supra* note 18, Annex III.

\(^\text{21}\) Hazboun, *supra* note 9, at 8.

\(^\text{22}\) *Id.* (noting that, as of December 20, 1993, "Palestinians and Israelis have not agreed on the mode of trade that will be sanctioned.").

\(^\text{23}\) Some commentators note a conflict between Israel's desire to maintain a customs union including Israel and the Palestinian Territories using Israeli customs duties and rules and the Palestinians' desire to have their own customs policy utilizing minimum tariffs to drop prices of imported goods in order to increase the average Palestinian's purchasing power. *Id.*
which first appeared in the Israel-PLO Agreement on the Gaza Strip and the Jericho Area ("Oslo I") and then in revised form in the Interim Agreement between Israel and the PLO on the West Bank and Gaza Strip ("Oslo II"). The Economic Protocol established a free trade area between Israel and the West Bank and Gaza and a customs union based on Israeli customs rules and tariffs rates. As traditionally understood, a free trade area is distinct from a customs union, which is sometimes also called a common market. While both a free trade area and a customs union attempt to eliminate duties and other restrictive regulations of commerce among the states involved, the customs union also involves harmonizing duties and other commercial regulations of all participating states that are applied against all other countries. In the negotiations on the Economic Protocol, the Palestinians pushed for a free trade arrangement while the Israelis wanted a customs union because they did not want to recognize Palestinian borders as would be required by a free trade area. The compromise reached in the Economic Protocol "borrows certain elements of both a common market and a free trade area agreement."

The first feature of this compromise is the freedom of movement of goods between Israel and the Palestinian Territories. The Economic Protocol allows Palestinian industrial and agricultural goods to move freely into the Israeli market. The Economic Protocol contains some exceptions to the free movement of agricultural goods, including the application of veterinary and phytosanitary measures and quotas on certain agricultural products that will be phased out by 1998. The free movement of goods between Is-

26. Oslo II, supra note 24, Annex V.
28. See, e.g., definitions of "customs union" and "free-trade area" in the General Agreement on Tariffs and Trade, art. XXIV(8)(a) & (b).
29. Kleiman, supra note 27, at 354-55.
30. Id. at 355.
31. Economic Protocol, supra note 24, arts. VIII(1) and IX(1).
32. Id., art. VIII(2)-(10).
rael and the Palestinian Territories promised to eliminate the discriminatory treatment suffered by Palestinian goods during the period of occupation. Palestinian enterprises would finally have significant access to the large Israeli market. The free movement of goods created by the Economic Protocol helped support the strategic objective of close economic relations between Israel and the Palestinian Territories.\footnote{See Fidler, supra note 3, at 537 (noting that "[t]he Economic Protocol enshrines a strategy of close economic contact and cooperation between Israel and the Palestinian Territories.").}

The second key feature of the trade provisions of the Economic Protocol is the establishment of a customs union involving Israel and the Palestinian Territories. Except in limited circumstances, the Economic Protocol commits both sides to using Israel's customs regime for imports.\footnote{Economic Protocol, supra note 24, art. III(1).} Thus, "Palestinian import taxes must generally be set no lower than the Israeli import taxes on equivalent goods."\footnote{Molkner, supra note 1, at 1447.} Diverging from a classic customs union model, the Economic Protocol allows the Palestinians to establish tariffs independently in two contexts: (1) specified goods produced in Jordan, Egypt, and certain other (mostly Arab or Islamic) countries may be imported subject to tariff rates set by the Palestinians up to "the Palestinian market needs" as determined by the two sides,\footnote{Economic Protocol, supra note 24, art. 111(2). Such goods are found in Lists A1 and A2 in Appendix I of the Economic Protocol. Id.} with imports exceeding the agreed amounts subject to prevailing Israeli tariff rates;\footnote{Id., art. III(10).} and (2) specified goods described as "basic food items and other goods for the Palestinian economic development program," may be imported without quantitative restrictions at tariff rates set by the Palestinians.\footnote{Id., art. III(4). Such goods are contained in List B in Appendix III of the Economic Protocol. Id.}

Another key feature of the Oslo Accords affecting Palestinian trade law is the power granted to the Palestinian Authority to negotiate agreements with states and international organizations to expand market access for Palestinian exports.\footnote{Oslo II, supra note 24, art. IX(5)(b).} Utilizing this power would help the Palestinian Authority fulfill the strategic economic development need for greater access to regional and global markets, which in turn would also help attract foreign inves-
tors who might be interested in the Palestinian Territories as an export platform.

In sum, the Oslo Accords established the framework for Palestinian trade during the interim period pending the final status negotiations. This framework has three major features: (1) free movement of goods between Israel and the Palestinian Territories; (2) the modified customs union between Israel and the Palestinian Territories; and (3) the authority of the Palestinian Authority to open export markets for Palestinian goods.

III. IMPLEMENTING THE OSLO FRAMEWORK FOR PALESTINIAN TRADE

In theory, the Oslo framework for Palestinian trade directly supported three of the four elements of the Palestinian economic development strategy. It provided the Palestinians with free access to the Israeli market, allowed the Palestinians to promote their exports regionally and globally, and established a trade situation that would help attract foreign investment because of access to Israel and potentially preferential treatment of Palestinian goods in other lucrative markets. The Oslo trade framework also indirectly supported the foreign aid component of the development strategy by creating an environment where private sector forces could effectively feed off the infrastructure developments made through aid.

Unfortunately, the implementation of the Oslo trade framework has not lived up to expectations. This section of the Article analyzes how the Oslo trade framework has broken down, contributing to the deterioration of the Palestinian economy and the erosion of the peace process.

A. Free Movement of Goods

The free movement of goods between Israel and the Palestinian Territories has never materialized largely because of Israel's security concerns. In response to Palestinian terrorist acts inside its territory and other perceived security threats, Israel has frequently closed its borders with the Palestinian Territories. These closures have wreaked havoc on the Palestinian economy. In the most recently available Quarterly Report on Economic and Social Conditions in the West Bank and Gaza Strip, the Office of the United
Nations Special Coordinator in the Occupied Territories ("UNSCO") reported that Palestinian real gross national product ("GNP") "has declined by 18.4 per cent between end-1992 and end-1996," which "is mainly attributable to the loss of employment in Israel and the decline in trade flows due to the Israeli closure policy." UNSCO also reports that the Israeli closure policy, combined with significant population growth, has caused real per capita GNP to fall 36.1 per cent between 1992 and 1996. In addition, UNSCO calculates that closures have cost the Palestinian economy approximately $6.5 billion for the 1993-1996 period, or a $4.4 million loss per day. Regarding Palestinian trade, the World Bank reported that:

Repeated border closures and stringent inspection routines added to the costs of Palestinian exports and undermined delivery schedules; as a result, merchandise exports fell by almost a half from 11 to 6 percent of GDP between 1992 and 1995. Imports also suffered, slipping from 46 percent of GDP in 1992 to 38 percent of GDP in 1995.

While the World Bank detected some encouraging trends in the Palestinian economy in early 1997, as Palestinian unemployment decreased and trade flows increased, it noted that the Israeli border closures after the March 21, 1997 terrorist attack in Tel Aviv reversed both these positive trends. Palestinian access not only to the Israeli market but also to foreign markets has been severely disrupted by the border closings. The border closures have even prevented Palestinians from conducting normal commerce between the West Bank and Gaza because safe passage through Israel between the two territories has been disrupted. The impact of the border closings on Palestinian

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41. Id.

42. Id.


45. Mel Levine, Palestinian Economic Progress under the Oslo Agreements, 19 FORDHAM INT'L L. J. 1393, 1406 (1996) (commenting on "the absence of safe passage between Gaza and the West Bank, which restricts even non-export oriented Palestinian producers to a fraction of their potential markets").
trade might be alleviated somewhat if Palestinians had their own international port rather than having to ship everything through Israeli points of entry and exit. Palestinian vulnerability to Israeli security actions will likely remain significant until the opening of the proposed airport and seaport in Gaza, scheduled for 1998.

The security-motivated border closings have also adversely affected Palestinian labor exports as Israel restricted the entry of Palestinian workers. The entry restrictions, moreover, form part of a broader Israeli government strategy to reduce systematically the role of Palestinian workers in the Israeli economy as part of the search for security. Reducing labor exports produces lower incomes in the Palestinian Territories, which has an adverse effect on consumption and savings. While the Economic Protocol did not guarantee the freedom of movement of labor between Israel and the Palestinian Territories, the economic effects of the border closures on earnings in the Territories have been painful. Likewise, the Palestinian terrorist acts in Israel have interfered with the free movement of goods and have undermined much of the economic development strategy for the Palestinian Territories. Access to the Israeli market and other regional and global markets has been frustrated. Foreign investors have been deterred by the disruption of trade caused by the border closures.

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47. SMALL BUSINESS SUPPORT PROJECT, HOW TO CONDUCT BUSINESS IN THE PALESTINIAN TERRITORIES 91 (1996) [hereinafter HOW TO CONDUCT PALESTINIAN BUSINESS].

48. Samir Abdullah, From the Editor, 1 PALESTINE ECON. PULSE 1,1 (Sept.-Oct. 1996) (noting that Israeli border closings “continue to restrict entry of Palestinian labour to the Israeli market”).

49. Molkner, supra note 1, at 1422. See also World Bank, West Bank and Gaza Update, supra note 44 (providing statistics on displacement of Palestinian workers in Israeli economy by other foreign workers).

50. UNSCO Quarterly Report, April 1997, supra note 40 (noting closures leading to declines in household living standards and in private sector investment).

51. Economic Protocol, supra note 24, art. VII(1) (granting each side the right to determine “the extent and conditions of the labor movement into its area”). See also Fidler, supra note 3, at 537-38 (discussing the Economic Protocol’s labor provisions).

52. See Levine, supra note 45, at 1405-06 (discussing how border closings have deterred foreign investors); Knudsen, supra note 4, at 22 (commenting on how violence made it “evident to many potential investors that the situation remains too uncertain and unstable for any major surge of private investment”); World Bank, The West Bank and Gaza:
with problems plaguing the aid program,\textsuperscript{53} the disrupted trade situation and the lack of foreign investment has eroded confidence in the entire peace process.\textsuperscript{54}

A smaller, but still frustrating, element of the breakdown of the free trade area has been the frequent use by Israel of non-tariff barriers to Palestinian trade.\textsuperscript{55} Such non-tariff barriers on Palestinian exports, particularly on those destined for third countries, have weaker security rationales. Responding to this problem, Levine has proposed that Israel "demonstrate convincingly that any burdensome border controls and port procedures that are in place are there solely for security purposes and not to create or preserve foreign trade advantages or domestic market controls."\textsuperscript{56}

The imbalance in the way the trade relationship between Israel and the Palestinian Territories operates has encouraged the Palestinian Authority to take action to create more opportunities for the Palestinian private sector. For example, in 1996 the Authority announced that "all foreign companies selling goods in Gaza and the West Bank must operate through a director importer, distributor or agent registered with the Palestinian Authority."\textsuperscript{57} The requirement to use a Palestinian-registered agent or representative has caused controversy in the Israeli business community that

\begin{quote}
\textit{Country Overview, supra} note 6 (noting that "[t]he West Bank and Gaza has not yet achieved the level of political stability required to attract major corporate investment").
\end{quote}

\textsuperscript{53} For discussions of the problems on aid, see Fidler, \textit{supra} note 3, at 540-43.

\textsuperscript{54} Knudsen wrote in 1996 that "[w]ith trade uncertain, private investment stagnant and donor aid slow . . . , the prospects of economic gains from peace materializing in the short term appear fanciful." Knudsen, \textit{supra} note 4, at 22.


\textsuperscript{56} Levine, \textit{supra} note 45, at 1407.

fears losing the Palestinian import market to Palestinian firms. According to the *Palestine Economic Pulse*, this new policy should theoretically benefit Palestinians "financially through the regaining of a market share" as regards imports and the subsequent marketing of such imported goods. While the new import agency policy might benefit Palestinian companies *vis-à-vis* Israeli firms, some in the Palestinian private sector are voicing concerns about the new policy leading to "distribution monopolies" created by the licensing scheme. It is still too early to tell what impact this new policy will have on the free trade area, and "[s]ome pessimism still remains regarding the ability of the PNA [Palestinian National Authority] to enforce this new regulation."

B. **Customs Union**

The customs union between Israel and the Palestinian Territories has not been successful either. As noted earlier, the Israelis and the Palestinians differed in the negotiations over the Economic Protocol as to the creation of a customs union. According to Molkner, "[t]he goal of the customs union is to prevent leakage of low-tariff imported goods from the Palestinian Territories into Israel." The impact on the Palestinians for accepting the customs union was higher prices for imported products because Israeli tariff rates are set higher than the Palestinians would set them if they had the ability to do so. These higher duty costs are passed onto the Palestinian consumer. While the Palestinians face higher costs for imports, the trade-off for them was the freedom of movement of goods into Israel and access for Palestinians to the Israeli labor market. Theoretically, the customs union was not optimal from the perspective of Palestinian economic development but was tolerable for an interim period because of the free movement of goods and the labor opportunities in Israel. In prac-

59. *Id.*
60. *Id.* See also infra note 146 and accompanying text.
62. See supra note 29 and accompanying text.
63. Molkner, *supra* note 1, at 1447.
64. *Id.* at 1448; Knudsen, *supra* note 4, at 21.
tice, the breakdown of the free movement of goods and labor opportunities has left the Palestinians bearing higher costs for imports under the customs union without the offsetting economic benefits. Thus, the customs union exacerbates the economic difficulties the Palestinians face.

Another adverse affect of the customs union on the trade framework established under the Economic Protocol is that it handicaps the Palestinian Authority's efforts to promote Palestinian exports. Molkner observes that the customs union "weakens [the Palestinian Authority's] capacity to negotiate favorable trade terms with third countries." The Palestinian Authority cannot offer third countries reduced tariff rates for their products because it is locked into the customs union driven by Israeli tariff duties. As a result, the Palestinian Authority cannot offer other states "favorable access to their domestic market as a quid pro quo for reciprocal access to a given foreign market." Unless Israel has a preferential trading arrangement with countries that may constitute markets for Palestinian goods, the Palestinian Authority is left to ask for non-reciprocal, preferential treatment for Palestinian goods. Unfortunately, many of the countries "that most interest Palestinian exporters are often countries with which Israel has little or no trade." Another way in which the customs union hurts Palestinian economic development is the fact that the tariff revenue unfairly accrues to the Israeli government rather than to the Palestinian Authority. Under the Economic Protocol, tariff duties paid on goods destined for the Palestinian Territories are to be allocated to the Palestinian Authority. The payment of tariff duties to the Palestinian Authority "is fundamental to the revenue performance of the PNA, which has surpassed all expectations and . . . was continuing to yield surprisingly buoyant receipts." Molkner notes, however, that the Palestinian Authority has lost "tens of millions of dollars of revenues" because Palestinian businesses have generally used Israeli importers, meaning that goods really destined for

66. Molkner, supra note 1, at 1448.
67. Id.
68. Id.
69. Id.
70. Economic Protocol, supra note 24, art. III(15).
the Palestinian Territories are marked as Israeli imports. Tariff revenue on such imports flows to Israel because the Economic Protocol only requires revenue to flow to the Palestinian Authority "when the final destination explicitly stated in the import documentation is a corporation registered by the Palestinian Authority and conducting business activity in the Areas." The loss of so much revenue makes the Palestinian Authority more dependent on aid for funding its activities. The change in the way imports into the Palestinian Territories are handled may affect the tariff duty payment problem. Under the new policy, all imports into the Territories will have to state explicitly that the final destination is "a corporation registered by the Palestinian Authority and conducting business activity in the Areas." Tariff revenues, thus, should flow more directly to the Palestinian Authority, reducing the amount of revenue now lost because of the dominance of Israeli importers in the Palestinian market.

Another problem with the customs union is that it encourages trade diversion—an economically inefficient outcome of trade policy. As noted earlier, the customs union applies a tariff rate that is higher than would probably exist if the Palestinian Authority set its own rates. The result is that imports are diverted from other and possibly more efficient sources to Israeli producers who have duty-free access to the Palestinian market under the Economic Protocol. Theoretically, the costs of trade diversion could be offset by Palestinian enterprises producing competing products, which would be trade creation. Palestinian enterprises have not, however, created much trade because of the breakdown of the free movement of goods, the lack of foreign investment, and the ineffective use of aid.

72. Molkner, supra note 1, at 1448.
73. Id.
74. Economic Protocol, supra note 24, art. III(15).
75. See supra note 57 and accompanying text.
76. Economic Protocol, supra note 24, art. III(15).
77. Palestinian Agencies: A Bitter Pill for Israel to Swallow, supra note 58, at 9 (discussing the impact of new Palestinian import agency policy on tariff revenue payments from Israel to the Palestinian Authority).
78. Molkner, supra note 1, at 1448 (noting that the customs union means that "the Palestinian customs rate is probably higher than it otherwise would be").
79. Ussama Dabbagh, Prospects for Trade in Palestine, 1 PALESTINE ECON. PULSE 14, 15 (July-Aug. 1996) (arguing that "[t]rade diversion has been caused by the imposition of Israeli customs tariffs on imports from the rest of the world").
80. Id. (arguing that higher cost imports "should have encouraged the substitution of such imports by domestic production in the [West Bank and Gaza Strip]").
The customs union also creates a more cumbersome set of mechanics for importing goods into the Palestinian Territories. An importer has to deal with three sets of rules: the Economic Protocol, the Israeli rules, and the Palestinian rules. Under the Economic Protocol, "[e]ach side will issue import licenses to its own importers . . . ." Under the new Palestinian import agency policy, the Palestinian Authority presumably will only issue import licenses to Palestinian-registered importers. The Palestinian Ministry of Economy, Trade, and Industry ("Ministry of Economy") issues import licenses for areas under the control of the Palestinian Authority; import licenses for West Bank areas still under Israeli control are issued by the Israeli Civil Administration. The Ministry of Economy must issue a license for each import shipment because of the quotas established in the Economic Protocol. For imports falling within the quota limits, the Economic Protocol imposes rules of origin on goods imported from Jordan, Egypt, and other Arab countries. For imports that fall outside of the Palestinian import quotas, Israeli customs law affects import shipments licensed by the Palestinian Authority because Israeli customs rules govern at that point. While this complex set of import rules does not create insurmountable obstacles to importing into the Palestinian Territories, the import mechanics are far from the "one stop" set of rules that would make Palestinian importing more efficient.

C. Promotion of Exports

The final element of the Oslo trade framework was the Palestinian Authority's power to negotiate agreements with countries to promote Palestinian economic development. To date, the results of the Palestinian Authority's efforts to gain access for Palestinian exports to regional and global markets are mixed. As mentioned earlier, the customs union has frustrated the strategy of promoting Palestinian exports because it limits what the Palestinian Authority can offer other countries in terms of access to the Palestinian market. Even the progress that has been made is undercut by

81. Economic Protocol, supra note 24, art. III (9).
82. See supra note 57 and accompanying text.
83. How TO CONDUCT PALESTINIAN BUSINESS, supra note 47, at 108.
84. Id.
85. Economic Protocol, supra note 24, art. III(8).
86. Id. art. III(10).
other circumstances or events that limit the near-term potential for large increases in Palestinian exports to foreign markets.

1. Regional Trade Arrangements

An obvious outlet for Palestinian exports is the markets of other countries in the Middle East. The World Bank estimated in 1993 that, absent the asymmetrical trading structure imposed on the Palestinian Territories by Israel during occupation, the West Bank and Gaza would have purchased only 36% of total imports from Israel (compared with the actual figure of 90% during the mid-1980's) and sold 20% of total exports to Israel (compared with the actual figure of 75% during the mid-1980's). The World Bank estimated that Palestinian trade with the rest of the Arab world absent the occupation's customs union would have been much higher, with 40% of Palestinian exports flowing to Arab countries. These World Bank calculations illustrate how significantly the occupation-era customs union diverted Palestinian trade away from the rest of the Middle East region to Israel.

The Palestinian Authority has been active in trying to create opportunities for Palestinian exports in the Middle East. The Palestinian Authority signed a Trade Cooperation Agreement with Jordan in 1995. According to the Palestinian Authority, this "agreement provides for certain preferential tax and customs exceptions for two-way trade with respect to fifty Jordanian and Palestinian products." While the Palestinian-Jordanian trade agreement seems limited in scope, part of the limitation stems from the Palestinian Authority's inability to change the tariffs imposed under the Oslo customs union. The Palestinian Authority can offer Jordanian goods only limited preferential treatment under the restricted areas in which the Palestinian Authority can establish tariff duties.

87. "Arab countries are a good target market for [Palestinian] industrial goods and services. This market represents $50-60 billion. Thus, capturing 1-2% of this market ... could mean a break-through for the Palestinian economy." Dabbagh, supra note 79, at 14.
88. WORLD BANK, The Economy, supra note 8, at 45.
89. Id.
90. Palestinian Trade: Terms of Reference, 1 PALESTINE ECON. PULSE 6, 6 (Sept.-Oct. 1996).
91. PALESTINIAN NATIONAL AUTHORITY, 2 INVEST IN PALESTINE: LAWS & REGULATIONS 26 (1995) [hereinafter INVEST IN PALESTINE: LAWS].
The Palestinian Authority and Egypt have signed an "interim cooperation agreement" on trade, but apparently this is not a formal trade agreement. 92 In February 1997, Egypt and the Palestinian Authority initialed an agreement that, among other things, committed them "to make a thorough study of a draft agreement regulating transport and transit trade between both countries." 93 The Oslo customs union will restrict, however, the ability of the Palestinian delegation to offer the Egyptians much in the way of preferential access to the Palestinian market.

It should also be noted that Israeli border closures and controls adversely affect Palestinian trade with Jordan and Egypt. As mentioned earlier, Palestinians have experienced problems with Israeli officials at crossing points into Jordan and Egypt. 94 Border closures have, of course, an even more adverse effect on Palestinian exports than routine Israeli non-tariff barriers. 95 Not only does the border problem inhibit the export potential of domestic Palestinian enterprises but it also deters foreign investors who were considering the Palestinian Territories as an export platform. 96

Despite the limitations imposed by the customs union and the border problems, the Palestinian Minister of Economy noted in late September 1996 that since the formation of the Palestinian Authority "there has been a new trend towards increased foreign trade with the Arab states." 97 The Minister of Economy also stated that the Palestinian Authority "is trying to increase its exports to Arab markets and in this context relies on Arab states granting preferential treatment of Palestinian goods, in line with

92. Palestinian Trade: Terms of Reference, supra note 90, at 6.
94. See supra note 55 and accompanying text.
95. See, e.g., Husam Abu Dagga, Gaza's High Value Added Crops—Export Potential, 1 PALESTINE ECON. PULSE 22, 22 (Sept.-Oct. 1996) (noting that Palestinian growers lost $3.45 million in revenues during the 1995-96 export season because of border closures during the carnation export season).
96. See Levine, supra note 45, at 1405 (describing a foreign investor interested in Gaza as an export platform to European markets who was deterred from actually investing by the risks associated with Gaza's borders).
97. Palestinian Economy Minister on Rising Budget Deficit, Falling Investment, BBC SUMMARY OF WORLD BROADCASTS, Oct. 1, 1996, available in LEXIS, News Library, Curnws File. The Minister of Economy noted that in 1995 the Palestinian Authority issued "310 licenses to import from Arab states . . . out of a total of 634" issued. Id. The Palestinian Authority issued 92 licenses to import from Jordan, 218 licenses to import from Egypt, and 324 licenses to import from other states in the world. Id.
the Saudi Council of Ministers' resolution to exempt Palestinian products from customs duty."

Even if the Palestinian Authority did not face the economic problems caused by the customs union and Israel's border policies, the Middle East may not be as promising for Palestinian exports as some might hope. The countries that fall within the Middle East and North African ("MENA") region share a number of characteristics that negatively reflect upon the MENA region's economic potential. MENA countries generally have high tariff rates to protect domestic enterprises, which discourages exporters in other MENA countries and eliminates the incentives for protected firms to be competitive by exporting to other regional and global markets. As a result, intra-regional trade within the MENA area is very low, accounting for only seven to eight per cent of total MENA trade. Unless the trade policies of MENA countries change dramatically, the MENA area may not offer much hope for Palestinian exports.

2. Trade with the European Union

Another potential market for Palestinian exports is the European Union. Since 1986, the European Union has provided trade concessions to certain Palestinian products. Under European Union regulations, "all Palestinian manufactured products enjoy free access to the Community market and key Palestinian agricultural products enjoy free access to the market." Dabbagh, supra note 79, at 15.

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98. Id.
100. WORLD BANK, CLAIMING THE FUTURE: CHOOSING PROSPERITY IN THE MIDDLE EAST AND NORTH AFRICA 16-17 (1995).
101. One Palestinian commentator noted this by arguing that "[a]ny feasible short term trade relations with Jordan require the removal or relaxation of existing regulations imposed by Jordan on Palestinian imports." Dabbagh, supra note 79, at 15.
102. INVEST IN PALESTINE: LAWS, supra note 95, at 26. The Palestinian Authority refers to these trade concessions as a trade agreement, id., but the concessions are unilateral actions of the European Union rather than formal agreements between the European Union and the Palestinians. The initial regulation in which preferential treatment was given to Palestinian products is Council Regulation 3363/86, 1986 O.J. (L 306) 103. Regulation 3363/86 was replaced in 1991 by Council Regulation 1134/91, 1991 O.J. (L 112) 1, which widened the scope of preferences for Palestinian agricultural products. In 1992, Council Regulation 190/92, 1992 O.J. (L 21) 7, instituted a tariff quota for Palestinian fresh strawberries.
tural products are granted . . . free or concessional access." Both the European Union and the Palestinian Authority demonstrated enthusiasm for building the existing trade concessions into a formal trade agreement, which came to pass in December 1996 when the European Union and PLO initialed the Euro-Mediterranean Interim Association Agreement on Trade and Cooperation between the European Community and the PLO for the Benefit of the Palestinian Authority of the West Bank and Gaza Strip. The Interim Association Agreement forms part of a larger European Union initiative called the Euro-Mediterranean Partnership launched in November 1995 that is designed to create a Euro-Mediterranean free trade area through successive bilateral Euro-Mediterranean Agreements between the European Union and countries in the MENA region. Prior to the Interim Association Agreement, the European Union had concluded Euro-Mediterranean Agreements with Israel, Tunisia, and Morocco.

The Interim Association Agreement involves more than the trading relationship between the European Union and the Palestinians because it covers a wide range of issues such as direct investment, capital movements, intellectual property protection, and political cooperation. While the entire Interim Association Agreement is important, this section will only briefly look at the trade-specific portions of it. According to the European Commission:

The main consequence of the agreement is the confirmation of a free trade area between the EC and the West Bank and Gaza Strip, in accordance with WTO rules.

103. Communication from the Commission to the Council and Parliament on Future European Union Economic Assistance to the West Bank and the Gaza Strip, COM(95)505 final, at 5.
107. See Interim Association Agreement in Proposal for a Council Decision concerning the conclusion by the European Community of a Euro-Mediterranean Interim Association Agreement on trade and cooperation between the European Community and the PLO for the benefit of the Palestinian Authority of the West Bank and Gaza Strip, COM(97)51 final [hereinafter Council Proposal].
The agreement commits the parties to the progressive establishment of a free trade area over a transitional period not extending beyond 2001, in conformity with the GATT.108

The Interim Association Agreement does not radically change the nature of trade between the Palestinian Territories and the European Union because trade between the two was already free by virtue of (1) the European Union’s granting of free access for industrial goods and preferential access for selected agricultural products from the West Bank and Gaza, and (2) the free trade arrangements already in place between Israel and the European Union.109 The dependence of the Palestinian Authority on Israel’s trade relations because of the customs union is illustrated by the Interim Association Agreement: without Israel’s existing free trade arrangement with the European Union, the Palestinian Authority has no power to grant the European Union reciprocal free access to Palestinian markets.

The potential economic impact of the Interim Association Agreement on the Palestinian Territories is uncertain. Prior to the Agreement, there was minimal trade between the European Union and the Territories.110 On the import side, the Agreement might produce lower cost imports as European Union imports force Israeli producers to face competition for the Palestinian market, thus creating efficiency-enhancing trade from the Palestinian perspective. On the export side, the benefits are unlikely to be significant because the Agreement does nothing to eliminate the obstacles that currently exist to Palestinian exports to the European Union, such as the breakdown in the free movement of goods from the Palestinian Territories to Israel. The negative effect of this breakdown on the prospects for Palestinian exports to the European Union also deters foreign investors from thinking of the Palestinian Territories as an export platform for European markets. Hoekman argues that “[t]he geographic advantage that the MENA region used to have—because Eastern Europe was effectively closed to open exchange with the West—has now disappeared.”111 The Central and Eastern European countries

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108. Id. at 1a. See also id. art. 3, at 5.
109. Id. at 1a-1b.
110. Id. at 1a (noting that trade “flows have in practice been small”).
111. Hoekman, supra note 99, at 1. Since the opening up of Central and Eastern Europe, the European Union has been pursuing trade liberalization strategies there and
("CEECS") are now reclaiming their geographical advantage, allowing them "to exploit sub-contracting of manufacturing products for export to the [European Union] to a much greater degree than the MENA countries."\textsuperscript{112}

Theoretically, the Euro-Mediterranean Partnership initiative could lead to an increase in Palestinian exports to other MENA countries for two reasons. First, the Euro-Mediterranean Agreements oblige MENA countries to liberalize their economies by reducing tariff rates \textit{vis-à-vis} the European Union, which will expose protected domestic industries to the forces of competition.\textsuperscript{113} If MENA governments were to extend this trade liberalization to other MENA countries, Palestinian exports could benefit from the resulting expansion of intra-MENA trade.

Second, the Euro-Mediterranean Agreements contain liberal rules of origin that allow the MENA party to count materials imported from other MENA countries as materials originating in the MENA party. For example, under the Euro-Mediterranean Agreement between the European Union and Tunisia, materials originating in Morocco (which also has a trade agreement with the European Union) shall be considered as originating in Tunisia for purposes of the European Union-Tunisian rules of origin.\textsuperscript{114} Under such liberal rules of origin, Palestinian exports to MENA countries party to Euro-Mediterranean Agreements might increase if they could be incorporated into products exported to the European Union without jeopardizing the products' preferential tariff treatment. Technically, the Euro-Mediterranean Agreement between the European Union and Tunisia does not accord Palestinian-originating products the benefit of the liberal rules of origin because it does not include the Palestinian Territories in the list of MENA countries to which the cumulative rules of origin apply.
The European Union and Tunisia might, however, allow Palestinian-originating products to benefit from these rules of origin. The Interim Association Agreement does not contain any provisions on cumulative rules of origin because Israeli customs rules largely control these questions under the customs union.\textsuperscript{115}

The theoretical possibility of increased Palestinian exports to other MENA markets is called into question, however, by the havoc created for all Palestinian exports by the breakdown of the Israeli-Palestinian free movement of goods. If Palestinian enterprises cannot physically deliver exports to customers in a timely fashion because of Israel’s security concerns, then customers will find more reliable foreign or domestic suppliers, and Palestinian economic development will continue to stagnate, which will further undermine the peace process.

3. Trade with the United States

The Palestinian Authority also has actively sought to promote exports to the United States. When the Palestinian Territories were under Israeli occupation, goods produced in the West Bank and Gaza and exported to the United States enjoyed the preferential treatment accorded to Israeli products under the United States-Israel Free Trade Agreement ("U.S.-Israel FTA") because they were marked "Made in Israel" and shipped to the United States through Israel.\textsuperscript{116} The peace process forced a change in this situation as Palestinians began to gain autonomy. In 1995, the U.S. Customs Service issued regulations requiring products from the Palestinian Territories imported into the United States to be marked either "Made in Gaza" or "Made in the West Bank."\textsuperscript{117} This change forced Palestinian products out of the preferential trading arrangement established in the U.S.-Israel FTA and gave Israeli products a competitive advantage over Palestinian products in the United States.

To offset the impact of removing Palestinian products from treatment under the U.S.-Israel FTA, the United States in 1995

\textsuperscript{115} See Interim Association Agreement, Protocol No. 3 Concerning the Definition of the Concept of "Originating Products" and Methods of Administrative Cooperation, in Council Proposal, supra note 107, at 49 et seq.

\textsuperscript{116} See New Marking for West Bank, Gaza Goods Omits Palestinian Goods from Israel FTA, 12 INT'L TRADE REP. 874 (1995) [hereinafter New Marking for West Bank].

extended preferential treatment to Palestinian goods under the U.S. Generalized System of Preferences ("GSP"). Palestinian officials, however, argued that GSP treatment would not provide economic benefits to the Palestinian economy because GSP excluded food and textiles—the very products that Palestinians could effectively export. Recognizing that the peace process was having the perverse effect of economically hurting the Palestinians for gaining some autonomy, the Clinton administration proposed extending duty-free treatment to all Palestinian products imported into the United States in exchange for duty-free access to the Palestinian Territories for American products. Legislation effectuating this proposal was introduced into Congress and eventually was passed and signed into law by President Clinton on October 3, 1996.

Technically, the legislation does not establish a free trade agreement. Rather, Congress has amended the United States-Israel Free Trade Area Implementation Act to authorize the President to proclaim elimination or modification of tariff duties for products originating in the Palestinian Territories. In essence, under this law the United States will treat Palestinian and Israeli goods equally—as it used to do during occupation. In return for getting duty-free access to the United States, the Palestinian Authority agreed to grant American products duty-free access to the Palestinian Territories as well as national treatment within them. The Palestinian Authority could make these undertakings because American products receive duty-free access to the Israeli market under the U.S.-Israel FTA, so the U.S.-Palestinian arrangement conforms with the Oslo customs union.

In announcing the new law, the White House stated that the "special trade status will provide new employment opportunities

119. New Marking for West Bank, supra note 116, at 874.
123. President Grants Duty-Free Entry to Products From West Bank, Gaza, supra note 121, at 1569. The undertakings from the Palestinian Authority were made in diplomatic correspondence with the United States in October 1995. Letter from Timothy Richards, Deputy Assistant U.S. Trade Representative for Western Europe and the Middle East, to David Fidler, Associate Professor of Law, Indiana University School of Law - Bloomington (Jan. 22, 1996) (on file with author).
for Palestinians outside Israel proper and lure increased foreign investment to the West Bank and Gaza.\textsuperscript{124} While it is too early to assess the accuracy of this prediction, Palestinian exports to the United States are subject to the same border closures as Palestinian exports to every other market. Access in theory to the United States will not provide employment or lure foreign investors while access in reality remains uncertain.

4. Palestinian Laws Affecting Exports

Attempting to build openings in foreign markets for Palestinian products has been the major emphasis of the Palestinian Authority in promoting exports. The Palestinian Authority has also attempted to create conditions within the Palestinian Territories to attract investments with export potential. The Palestinian Law on the Encouragement of Investment allows the Palestinian High Agency for the Encouragement of Investment to grant special incentives to "export projects" and to "export-oriented agricultural projects."\textsuperscript{125} The authority to grant such special incentives "suggests that the PNA wants to adopt an 'export model' of economic development as opposed to an 'import substitution' model ...."\textsuperscript{126} The Palestinian Authority does not require the exportation of products for investment approval, which is in keeping with international standards on trade-related investment measures.\textsuperscript{127}

The Palestinian Authority has also established the mechanics needed to engage in an export transaction. The Ministry of Economy has, according to the Palestinian Authority, simplified export procedures "to encourage and promote exports."\textsuperscript{128} The Palestinian Authority claimed in its official documents distributed at the second MENA conference in 1995 that no export license is needed; merely an official certificate of origin certifying that the goods are of Palestinian origin is required.\textsuperscript{129} A guide to conduct-

\textsuperscript{125} Law on the Encouragement of Investment, art. 12, reprinted in Fidler, supra note 3, at 607. For a critical analysis of article 12, see Fidler, supra note 3, at 564-66.
\textsuperscript{126} Fidler, supra note 3, at 566.
\textsuperscript{127} Id. at 581.
\textsuperscript{128} INVEST IN PALESTINE: LAWS, supra note 91, at 26.
\textsuperscript{129} Id. See also MAZEN E. QUFTY ET AL., LEGAL ASPECTS OF DOING BUSINESS IN PALESTINE 45 (1995) (stating that no export license is needed, only a certificate of origin). This certificate of origin is very important in establishing that the Palestinian export can
ing business in the Palestinian Territories, funded by the U.S. Agency for International Development ("USAID") and published in January 1996, states, however, that Palestinian exporters need both an export license and the certificate of origin. This guide even provides a copy of the official Ministry of Economy export license application.

Either the Palestinian Authority changed the rule between the second MENA conference in November 1995 and the publication of the USAID handbook in January 1996, or it needs to be more accurate about its simplified export procedures.

D. Industrial Zones

The need for Palestinian economic development, combined with the continuing lack of such development, has led to searches for ways to "jump start" trade with and investment in the Palestinian Territories. The World Bank, Palestinian Authority, Israel, and donor countries like the United States have been developing plans for a number of industrial zones in the West Bank and Gaza that are supposed to act as economic catalysts for the Palestinian economy. The World Bank reports that the Palestinian Authority and Israel have agreed to cooperate on three industrial zones—one at Carni in Gaza and two in the West Bank at Jenin and Tulkarem. The industrial zones program seeks "to create a number of 'islands' of procedural and legal clarity that will also be assured exceptional security treatment." This program thus responds to the general problems of security (discussed above) and the lack of an adequate Palestinian commercial law framework (discussed below). The planned industrial zones figure prominently in Palestinian trade hopes because products produced in the zones are supposed to have more secure access to the Israeli market and will get duty-free treatment into the United States and the European Union, making the zones "attractive 'export platforms' to those markets."

benefit from preferential trading arrangements, like with the United States or the European Union, because such arrangements will have specific rules of origin.

130. HOW TO CONDUCT PALESTINIAN BUSINESS, supra note 47, at 102-03.
131. Id. app. E(8).
133. Id.
134. Id.
135. Id. See also Julian Borger, Clouds over Middle East Peace: Trade in the West Bank is Exposed to Israeli Sanctions, THE GUARDIAN, July 23, 1997, at 18 (reporting that "[t]here is interest in the [Carni, Gaza] zone from European and US investors who want
The industrial zones sound good in theory, but the actual implementation of the theory has been delayed and still remains elusive. The idea of industrial zones has been around since early in the peace process, but nearly four years later the Palestinians and Israelis have not concluded the necessary agreements, nor have the Palestinians completed drafting the legal framework for the zones. Although talks on the industrial zones between the Israelis and Palestinians have continued despite the freeze in the peace process, any major economic impact from the zones is still a distant prospect. Palestinian businesspeople have grown more frustrated with the "continuous squabbling between Israeli and Palestinian negotiators over who will control the flow of goods and people" through the industrial zones. Some Palestinian businesses purposefully avoid the industrial zones because they have become "tinged [with] political concerns." The "islands" of legal clarity, assured market access, and special security treatment are in danger of being covered by the stormy waters of the peace process.

E. Legal and Political Problems

In addition to the issues raised previously, a number of legal and political problems also adversely affect the prospects for Palestinian trade. While a full discussion of these problems is beyond the scope of this Article, it is nonetheless important to raise them, however briefly.

1. Inadequate Legal Infrastructure

A continuing problem for prospects for Palestinian economic development is the inadequate nature of the legal infrastructure to benefit from the territories' low labour costs and preferential access to EU and US markets.".

136. World Bank, West Bank and Gaza: Country Overview, supra note 6 (reporting that the Palestinians are still drafting the legal framework and discussing market access agreements with Israel).

137. Borger, supra note 135, at 18.


139. Id.
for conducting business in the Palestinian Territories.\footnote{140} In 1993, the World Bank reported that "[d]espite some improvements in the recent past, there remains a widespread perception among OT entrepreneurs that the current business environment is ambiguous, complex and unpredictable."\footnote{141} The World Bank expressed the hope in 1993 that the peace process "should make possible a thorough review and overhaul of the existing legal and regulatory framework to provide the private sector with a sounder legal basis for commercial transactions."\footnote{142} This hope has not been fulfilled. In a recent 1997 overview of the West Bank and Gaza, the World Bank stated that "[i]n addition to political uncertainty, the business environment suffers from confusing commercial legislation and a lack of public sector regulatory institutions."\footnote{143} Even in some areas where the Palestinian Authority has tried to reform Palestinian commercial law, the results have not been encouraging. When the Palestinian Authority issued the Law on the Encouragement of Investment, "World Bank experts, lawyers working to promote the peace process, international legal scholars, and potential foreign investors quickly perceived that the Investment Law was a very flawed document."\footnote{144} While the consequences of terrorist acts and subsequent border closings no doubt complicated Palestinian legal reform efforts, the blame cannot be laid entirely at Israel's doorstep. In connection with the Law on the Encouragement of Investment, for example, the timely and adequate drafting of this major piece of legal reform "was in the hands of the Palestinians themselves, and they had an opportunity to demonstrate to the world that they understood the importance of foreign direct investment to the achievement of peace and Palestinian autonomy."\footnote{145} As suggested by the World Bank's recent comment

\footnote{140}{For an overview of the need for Palestinian legal reform, see Hiram E. Chodosh and Stephen A. Mayo, \textit{The Palestinian Legal Study: Consensus and Assessment of the New Palestinian Legal System}, 38 HARV. INT'L L. J. 375 (1997).}

\footnote{141}{\textsc{World Bank, Overview}, supra note 5, at 17.}

\footnote{142}{Id.}

\footnote{143}{World Bank, \textit{The West Bank and Gaza: Country Overview}, supra note 6. The World Bank has proposed for its 1997 fiscal year a Legal Development Project to "support the modernization and harmonization of existing legislation, the improvement of judicial infrastructure, the development of legal information and training and technical assistance for judges and court personnel." \textsc{World Bank, West Bank and Gaza Update: January-March 1997}, supra note 44.}


\footnote{145}{Id.}
about confusing commercial legislation and the lack of public sec-
tor regulatory institutions, the story of the Law on the Encour-
agement of Investment is not unique in connection with Palestin-
ian legal reform.

2. Trade Monopolies

Even more disturbing than the problems concerning needed
commercial law reform is the Palestinian Authority’s practice of
creating trade monopolies for itself. The Palestinian Authority
exclusively controls, for example, the importation of many prod-
ucts, including cement, petroleum, and flour. In some situations,
Israel supports these trade monopolies in order to protect Israeli
suppliers from competition in the Palestinian market. In addi-
tion, not all the revenue generated by these trade monopolies goes
to the Palestinian Authority and private enterprises because Ara-
fat reportedly takes a cut of the money.

Concerns about the attempts by the Palestinian Authority to
monopolize sectors of the Palestinian economy are commonplace
among investors and groups trying to facilitate the peace process
and Palestinian economic development. In a letter to President
Clinton dated April 4, 1997, the Israeli director of the widely-
respected, Bethlehem-based Israel/Palestinian Center for Re-
search and Information urged the United States to use its influ-
ence to put an end to monopolistic Palestinian Authority policies
that “will strangle the private sector and delay or prevent eco-
nomic development.” Palestinian Authority attempts to mo-
nopolize aspects of the Palestinian economy are thus not hidden
secrets. Such behavior on the part of the Palestinian Authority di-

147. Id. “The Government of Israel should not allow or facilitate the establishment of
monopolistic economic policies involving Israeli companies and supported by the Pale-
stinian Authority. This is detrimental to the Palestinian economy and has created great
resentment within Palestinian business circles as well as on the ground in the West Bank
and Gaza.” Gershon Baskin, Recommendations on Steps to be Taken with Regard to Pal-
estinian Economic Development Needs in Relationship with Israeli Security Needs, IPCRI
Memorandum, November 3, 1996 (on file with author).
148. “For example, out of the $74 for which a ton of cement is sold in Gaza, $17 goes to
the Authority and $17 into his own [Arafat’s] account in a Tel Aviv bank.” Hirst, Sham-
less in Gaza, supra note 146, at T8. See infra, text accompanying notes 150-157
149. Letter to President William Jefferson Clinton from Gershon Baskin, Israeli Direc-
tor of the Israel/Palestinian Center for Research and Information, April 4, 1997 (on file
with author).
rectly calls into question its commitment to free market enterprise as the model for Palestinian economic development and casts a dark shadow across Palestinian trade efforts.

3. Corruption

The lack of an adequate and functioning system of commercial law, combined with heavy government intervention in the economy, is a recipe for corruption. The Palestinian Authority is rife with corruption. Rumors about corruption have plagued the Palestinian Authority since its establishment, but what was widely suspected dramatically broke open to public disclosure in the first half of 1997. In early April, the Israeli newspaper *Ha'aretz* published a report detailing secret bank accounts in Tel Aviv used by Arafat and other senior Palestinian officials. Later in April, David Hirst of *The Guardian* newspaper in Britain published a detailed story on the extent of corruption in the Palestinian Authority. Hirst’s investigations led him to a blistering conclusion: Arafat “and his coterie of unofficial economic ‘advisors’ have thrown up a ramshackle, nepotistic edifice of monopoly, racketeering and naked extortion which merely enriches them as it further impoverishes society at large.”

Finally, in May 1997, the Palestinian Authority released an internal audit of corruption that reported that corruption and mismanagement caused the Palestinian Authority to lose approximately $326 million in public funds, representing 40 percent of the Palestinian Authority’s annual budget. Perhaps the public disclosure of the corruption problem, and the anger it has caused among Palestinians and donor countries, will bring corruption under control. The Palestinian Legislative Council has published a report that severely criticized Arafat’s cabinet and called for Arafat to replace all cabinet ministers in an effort to bring credibility and accountability to the Palestinian Authority. Sixteen of the eighteen members of Arafat’s cabinet have offered to resign as a result of the corruption scan-

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151. Hirst, Shameless in Gaza, supra note 146, at T8.
154. Id.
In addition, "international donors, mostly from the European Union, threatened to cut off $1.4 billion of aid pledged but not yet paid to Palestine when they got wind of the extent of the [corruption] problem." The scandal has tarnished the Palestinian Authority and further hurt prospects for Palestinian economic development.

4. Human Rights Abuses

The reputation of the Palestinian Authority has also been damaged by the revelations of human rights abuses committed by the Authority. In December 1996, Amnesty International released a report on the human rights performance of the Palestinian Authority since 1994. Amnesty International's conclusions were disturbing:

Over the past two years widespread human rights abuses have taken place in the areas under the jurisdiction of the Palestinian Authority including large-scale arbitrary arrests, prolonged detention without charge or trial of hundreds of political detainees and the increasingly widespread use of torture. At least nine people have died in the custody of the Palestinian security services in circumstances where torture appears to have caused or contributed to their deaths. Those brought to trial for political offenses have been almost invariably tried before a State Security Court which allows summary, unfair and often secret trials of offenders before military judges. Other serious human rights abuses include unlawful killings and possible extrajudicial executions.

The sting of the Amnesty International report apparently did not register with Arafat and other Palestinian officials because subsequent events have illustrated a lack of appreciation in the

156. Id.
157. Neil MacFarquhar, *The Sullen Zone: As Gaza Stagnates, Arafat is Blamed as Well as Israel*, N.Y. TIMES, Aug. 16, 1997, at 1 (noting that corruption and mismanagement are not only making donor countries reconsider aid pledges but are also deepening the qualms of the private sector about investing and doing business in the Palestinian Territories).
159. Id. at summary.
Palestinian Authority for human rights. First, the Palestinian Authority declared in April 1997 that any Palestinians who sell land to Jews would be punished by the death penalty.\textsuperscript{160} This declaration led to the deaths of at least three Palestinian real estate agents suspected of selling land to Jews,\textsuperscript{161} and dozens more have been "arrested and threatened with execution."\textsuperscript{162} This episode prompted international criticism, including a U.S. House of Representative's vote condemning the Palestinian Authority for the killings.\textsuperscript{163}

Second, Arafat ordered the detention in May 1997 of Daoud Kuttab, a Palestinian journalist who was directing live television broadcasts of the Palestinian Legislative Council.\textsuperscript{164} Arafat apparently was unhappy with Kuttab's live broadcasts because the Legislative Council had been critical about the Palestinian Authority over corruption issues.\textsuperscript{165} The detention of Kuttab aroused fierce opposition in the United States and elsewhere. A \textit{Washington Post} editorial stated that the Kuttab affair is "certain to put Yasser Arafat's increasing despotism squarely in the American public eye."\textsuperscript{166}

The human rights abuses directly attributable to the Palestinian Authority give it a menacing, authoritarian image that adversely affects prospects for Palestinian economic development. Dictatorships and kleptocracies have historically proven to be maladroit at promoting trade and investments.

IV. CONCLUSION: NO PEACE, NO TRADE—NO TRADE, NO PEACE

Analyzing the developments in Palestinian trade law during the peace process points to a very daunting conclusion: without more peace between Israel and the Palestinians, Palestinian trade will remain uncertain because of its vulnerability to Israeli security ac-


\textsuperscript{161} Joel Greenberg, \textit{As Fear Spreads, Palestinian Land Broker Tells of Abduction}, \textit{N.Y. TIMES (INT'L)}, June 4, 1997, at A12.

\textsuperscript{162} Beyer, \textit{Let the Seller Beware}, supra note 160, at 40.


\textsuperscript{165} Id.

tions; but without more trade, the Palestinian people will continue to lose confidence in the peace process as unemployment, poverty, and despair create fertile ground for forces opposed to rapprochement with Israel. As Mel Levin has argued, the Israeli security concerns and the Palestinian economic needs are both legitimate.\textsuperscript{167} Levine sets out the mental framework needed to break the downward spiraling cycle of "no peace, no trade—no trade, no peace":

Realism dictates that both sides must enter a quest for creative solutions with an honest acceptance of one another's core requirements. This means that the Palestinians must accept, as a minimum, that "free movement" is not exclusively, or even primarily, an economic issue, and that the Israelis must accept the presence of a determined economic partner and competitor on their doorstep. Good faith may or may not follow, but without these going-in positions on both sides, it is prohibited.\textsuperscript{168}

In addition, the Palestinian Authority has to improve vastly its performance by reforming its commercial law to conform to international standards, ending government trade monopolies, eliminating corruption, and moving towards firm protection of human rights.

The strategy for Palestinian economic development crafted by the peace process pioneers was eminently rational and logical: build a modern infrastructure using aid, access the lucrative Israeli market, attract foreign investment, and develop an export-oriented economy. As noted earlier, access to the Israeli and other markets is essential to trade, and the opportunity to trade is critical to prospective foreign investors. The implementation of the economic development strategy through the Oslo Accords followed three rational and logical channels: the free trade area, the customs union, and Palestinian authority to promote exports. Unfortunately, the strategy and the implementation mechanisms for it have proved to be as fragile as a house of cards. As Kleiman observed in 1994, "[c]oupled with severe, or even absolute restrictions on the entry of labour, frequent closures can play havoc with the economic logic underlying the whole agreement."\textsuperscript{169}

\textsuperscript{167} Levine, \textit{supra} note 45, at 1406 (noting that the situation "is a classic political/economic conundrum").

\textsuperscript{168} \textit{Id.} at 1408.

\textsuperscript{169} Kleiman, \textit{supra} note 27, at 372.
The collapse of the Palestinian economic development strategy has led many to start speculating about the best way to re-cast Palestinian trade law in the final status negotiations. Ussama Dabbagh has argued, for example, that Palestinian trade policy should involve four elements: (1) protection or subsidization of some Palestinian industries; (2) imposition of discriminatory tariffs on Israeli imports; (3) movement towards a customs union with Jordan; and (4) development of markets for Palestinian products outside the Middle East.\(^{170}\) The thrust of Dabbagh's recommendations is separation of the Palestinian Territories from Israel, which is a theme others have sounded.\(^{171}\)

Geographic realities make such a separation virtually impossible. Further, the Israeli economy is too big and too important in the MENA region to eliminate it as a part of the Palestinian economic development strategy. A more realistic trade strategy would entail two basic elements. First, the Palestinian Territories desperately need their own ports of exit and entry not subject to Israeli security actions or non-tariff barriers. Plans to complete such facilities in Gaza need dramatic acceleration. Further, in the permanent status negotiations, the Palestinians need to gain more control of their borders with Egypt and Jordan so that trade can flow more easily to and through these countries. In an age where many pundits and politicians are fervently discussing the development of the "borderless world," it seems odd to advocate that in order to join such a borderless world, the Palestinians need their own borders. Borders still matter, however, particularly if a nation does not control any.

Second, the free trade area plus customs union arrangement needs to be replaced with a straight free trade agreement between the Palestinians and Israel. This change would allow reciprocal preferential treatment of imports as exists under the Economic Protocol but would allow the Palestinians to set their own tariff rates with the rest of the world. Having the power to establish tariffs would give the Palestinians more to bargain with when trying to pry open foreign markets. The Palestinians could, thus, solidify the free trade arrangements already concluded with the United States and with the European Union. Palestinian control

\(^{170}\) Dabbagh, supra note 79, at 16.

\(^{171}\) See, e.g., Shlomo Avineri, Sidestepping Democracy, 73 FOREIGN AFF. 12, 14 (July/Aug. 1994) (advocating that the Palestinians build their economy "with as few links to Israel as possible").
over their tariff rates could also allow the Palestinians to be a voice for more trade liberalization in the MENA region. Israeli concerns about the Palestinian Territories becoming a conduit for cheap goods into Israel would have to be dealt with through specific rules of origin in the free trade agreement, perhaps modeled on the rules of origin in the U.S.-Israel FTA.

If the final status negotiations produce a Palestinian entity with international legal status, then a further element of a re-cast Palestinian trade policy would be membership in the World Trade Organization ("WTO"). The WTO would impose healthy disciplines on Palestinian trade law that would keep it firmly on the liberal, market-oriented path Palestinian leaders claim they want to walk. It would also give the Palestinians a seat at the global trading table like every other sovereign nation.

In essence, my proposal advocates dismantling the hybrid free-trade area/customs union created in the Economic Protocol. While the customs union model clearly dominates the Economic Protocol, the free trade area model takes precedence in my proposal. The free trade model requires, of course, that borders between Israel and the Palestinian Territories exist. Fixed borders are, of course, consistent with the goals of the permanent status negotiations in which the controversy concerns where to fix borders rather than whether to fix them. At issue too in the negotiations will be the border powers of the Palestinian Authority. My proposal advocates that these powers at least ought to include customs authority sufficient to operate a free trade area with Israel—collecting duties and verifying compliance with rules of origin, etc.

I realize that my recommendations rest on an assumption of peace, just like the economic strategy developed by the leaders who crafted the peace process and the Oslo framework for implementing the economic development strategy. Events during the life of the peace process have treated this assumption cruelly. Although Secretary of State Albright's intervention may have halted the peace process' free fall following the September 1997 suicide bombing in Jerusalem, it still remains to be seen whether the peace process will recover any of the ground lost in recent years. The hostility that has grown between Israel and the Palestinians and the manifest failures of the Palestinian Authority on economic and political issues perhaps make it look rather foolish to continue holding the assumption of peace. But this assumption is also a faith in humanity that history may treat roughly but can never extinguish. My analysis of Palestinian trade law and my argument
for a change in the arrangement established in the Economic Protocol assumes that the peace process will survive in some form because neither the Israelis nor the Palestinians want to return to the torments of the occupation. In analyzing Palestinian trade law, I walk, however feebly, down the path less traveled in the Middle East. Perhaps continuing to choose this path will one day make all the difference.