A Reevaluation of the Border Industrial Estates Concept

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Introduction

This paper is aimed to serve as an evaluation of the concept of border industrial zones between Israel and Palestine. The paper examines the way they developed and what some of the prospects and problems the first zone, the Gaza Industrial Estate (GIE), is confronting with regard to attracting investors. The Gaza Industrial Estate is meant to serve as a model of economic development in the Palestinian Authority areas and a model for economic cooperation between the PA and Israel.

This paper looks mostly at the prospects for attracting Israeli investors. One of the main investors or potential group of investors in the border industrial zones should for obvious reasons be Israeli companies. He high potential of attracting Israeli investors was further substantiated by a study IPCRI conducted for the World Bank in May 1995 in which we tried to identify potential investors and to identify their particular concerns regard to the possibilities for implementing their investment potential. That study found that the group most likely to invest in the GIE was the group of Israeli industrialists.[1]

Background

[1] Investor Research Project for Industrial Free Zones in the West Bank and Gaza, May 14, 1995. This research was conducted by a team set up by IPCRI under the title: Palestinian Israeli Peace Economists Consortium, Jerusalem. Ten of the twenty-seven Israeli industrialists interviewed indicated a significant interest in possible investments in Palestinian industrial zones.

The idea of the Palestinian-Israeli border industrial estate first emerged in discussions between the Palestinians and the Israelis in late 1993 to mid-1994. Mr. Abu Ala, then the chief negotiator on the Palestinian side, Ambassador Dennis Ross, and Mr. Uri Savir, the Director-General of the Israeli Foreign Ministry, formed a trilateral committee which evaluated the possibilities of economic improvement on the Palestinian side and economic integration between Israel and the emerging Palestinian entity.

The initial idea was developed because of the dissatisfaction in Israel with more than 150,000 Palestinian day laborers crossing into Israel daily. Rather than having thousands of Palestinians leave their houses every day after midnight and return home late in the evening, investments should bring employment to the Palestinians by means of establishing cooperative face-to-face border industrial estates.

Discussion started to take place in the Israeli and Palestinian economic the political communities. On the Palestinian side, there was one interest group that totally rejected the idea and another that supported the idea. On the Israeli side, those supporting the idea came from the Finance Ministry while those opposed were in the Ministry of Industry and Trade.

The initial concept involved taking two pieces of land on the border between the Palestinian Authority and Israel and merging this piece of land for the industrial estate. However it was thought that it was not possible from the legal standpoint because the land on the Israeli side would be governed by Israeli law and the land on the Palestinian side would be governed by the Palestinian legal framework or law.

On the Palestinian side, the idea of face-to-face industrial zones was regarded as premature in terms of cooperation with the Israeli economic and political establishment. It was also looked at as giving up land that would be taken by the Israeli side. It was seen as impractical. Palestinians believed that without unifying the two pieces of land that would be set aside for the joint program, it would be difficult to establish a unified regime. When conceptualizing an industrial estate it requires a single, unified legal framework, a unified incentive package or packages, a unified management team and a unified set of infrastructure services.

With regards to an incentive package, the Israeli investment promotion law provides a very generous subsidized investment incentive package- 24 to 29 percent in grants and loans on capital investments. The Palestinian Authority did not have any money at that stage to provide any subsidies or grants. Therefore, it was not possible to promote or achieve a unified incentive package unless the Palestinians would give control of their part of the estate to be located in area A, thereby using the Israeli legal framework and their incentive .

Facing these three difficulties, and after much discussion, the proposed solution agreed upon was that the Palestinian Authority would provide space on the Palestinian side of the border and thus the definition of the concept changed from a face-to-face industrial estate to a border industrial estate on the Palestinian side only.

In mid-1994 the Israelis and Palestinians, in reflection of the optimism about the peace process that existed then, spoke about nine industrial states, three in Gaza and six in the West Bank. However, shortly after arguments emerged on identifying the various site locations, they realized they could not move ahead so rapidly with so many projects all at once. There was no financing and no political will on the Israeli side to support nine industrial states. The final discussion in the trilateral committee agreed to three industrial states. They decided that one would be in Gaza and two would be in the West Bank.

The Palestinian economic establishment in the private sector criticized the Authority for introducing a concept which seemed only to service the needs of the Israeli economy. Border industrial estates, whether on the Palestinian side alone or face-to-face, were accused of being of service to the Israeli side, of providing a solution to the issues of cross-border mobility and closures. The Palestinian Ministry of Economy was accused at that point of not addressing the actual economic and investment-enabling environment in the industrial sector in Palestine, but rather trying to solve a problem of the Israelis.

At this stage, the World Bank got more involved in the issue of industrial estates. They prepared a document which was presented in a consultative group meeting of the Donor Nations, in which they evaluated the possibility of success of such a program[2]. They recommended going with one project as a pilot program. They looked at the possibilities and saw the Gaza industrial estate as being the most appropriate site because of the severity of unemployment in Gaza, because the site is area A, because the site is on the border and because there was an investor willing to take over the development of the site[3]. That is how the Gaza industrial estate as a project was born as the first pilot industrial state project. Jenin was the second project, but Jenin faced -- and is still facing -- lots of problems mainly because the land purchased for the project is located in Israeli

At the end of 1994, the Palestinian investment group PADICO began discussions with the Palestinian Authority on the Gaza industrial estate. In mid-1995, a document was drafted between PADICO and the Palestinian Authority defining the terms of reference of the responsibility of the development. The PA did not have the money and the experience to manage an industrial state, and therefore, PADICO was granted the license and rights to develop, market and manage the site.

PADICO began the design in late 1995, started development in the third quarter of 1996, and at the end of 1998 Phase I of the Gaza industrial estate was ready for occupancy.

The Gaza Industrial Estate (GIE)

The Gaza industrial estate is 485 dunams, 485,000 square meters utilizing a concept of 30/70 - green and service areas with 212 sites to be developed in this piece of land.

[2] Investor Research Project for Industrial Free Zones in the West Bank and Gaza, May 14, 1995. This research was conducted by a team set up by IPCRI under the title: Palestinian Israeli Peace Economists Consortium, Jerusalem

[3] PADICO

There will be three types of services provided in terms of industrial lots: steel structures in three sizes -- 600 square meters, 1200 square meters and 2,100 square meters; concrete multi-story buildings for software-oriented and textile-oriented industries; and lots for specialized industries with special designs.

The estate will be serviced, according to PADICO, with the best
ovided
by the United States, the World Bank and the European Investment Bank. An amount totaling about $24.5 million was provided. This money was -- and is -- being used to provide roads, telecommunication, water, sewage treatment and solid waste management to the estate.

PADICO, in its marketing pitch claims that it has developed the estate based on the best international standards. Each lot will be provided with all infrastructure services. There will be a one-stop window on-site for all services required for a business to exist in the industrial estate located there. The estate will include a training center, and a labor recruitment facility. PADICO realizes that they have many impediments to deal with,
these by very developed, very well-designed services that would offset the problems that people perceive in
[4].

is a problem, you do not have to deal with them. We will process your application as developer and manager of the park. We will submit your application and get you the license to do business. If you do not want to go into Gaza to recruit labor, we will do that for you. We will have a recruitment center. If you want to train your laborers, we will do that for you. We will provide you either with the space or with the space and trainers. If you need any service from the local business community, we

[4]Dr. Amin Haddad, Director of Public Relations for PADICO, October 1998 at an IPCRI sponsored Roundtable Meeting on the Future of the Border Industrial Estate concept.

will provide you with that. We will either introduce you to the local [5]

The cost of the project in totality was $65 million. Forty million dollars were provided by the company, the Palestine Industrial State Group, a subsidiary of PADICO, and $25 million was provided by the Palestinian Authority through the support of the donor community. The World Bank provided the Palestinian Authority with $10 million in a soft loan. The Americans provided $6.5 million. The European Investment Bank provided another loan in the size of $4.5

The Challenges

The GIE management claims to have already signed memoranda of understanding with some 12 companies, including two Israeli companies. There is no doubt that there is a large amount of competition in the world today for attracting investments and the state of the global community is not the best for attracting new investors. The potential of the Israeli investors has not been reached by the Gaza Industrial Estate. More than sixty Israeli companies with money to invest have pursed, even aggressively, the possibility of entering the GIE, yet only two have so far been reported to do so.

IPCRI already assumed in 1995 that the main problem facing the border industrial zones with regard to potential Israeli investors would be two-fold (and inter-linking): uncertainty regarding the legal framework, and a lack of trust in the general rule (or lack) of law under the Palestinian Authority. The first reference is to the lack of modern laws protecting the rights of the investors including a progressive law for capital investment, an Industrial Estates Authority law, a tax law, and even a company law. With regard to the relationship to the rule of law, there is still an undeveloped

[5] Ibid.

court system and little possibility to guarantee the enforcement of court decisions and of contracts.[6]

Israelis are easily willing to give up their legal framework. The government may present a position that is politically opposed to giving up the Israeli legal framework in some case or another. But that is not the difficulty with industrial parks. The resistance of the Israelis should be looked upon as a collective reaction of individuals and businesses. It is the individual businessman that is unwilling to give up the right to mitigate differences, to settle differences, to face the unions, the tradesmen or whoever, outside the Israeli legal framework which includes the courts and includes a very complex and highly developed system of mediation. This is especially the case when the alternative is not at all clear.[7]

in the short history of the Palestinian independent entity is rejecting or discarding the prevailing legal system when the Authority came into being, and/or not adopting an existing developed legal framework. It takes something like ten, twenty, thirty years, to develop a reliable and trusted legal regime. The trouble with the whole idea is that too much attention has been paid to the physical, material hardware, and too little to the question of

[6]Israeli investments have been made in Jordan where there is a solid and sturdy legal framework and where the Rule of Law has a proven history. It should be noted that the investments in Jordan could have been made in Gaza but in

the main reason for preferring Jordan over Gaza was precisely this issue of the legal regime despite that the physical difficulties for the Israelis of running their

interviewed expressed any second thoughts on this matter.

[7]In the survey conducted by IPCRI for this paper amongst potential Israeli investors, it is clear that the overwhelming number of those surveyed declared the legal framework to be the single most important factor for them in making a decision about investments in the Palestinian areas.

the software. That can be corrected by the government, of course -- the [8]

What Must Be Done

The Israeli government can provide guarantees or insurance to individuals as well as other means of facing difficulties in case of distress resulting from labor disputes, which are almost inevitable, free zone or no

interfere. There are tradesmen and there will be tradesmen and there is no way you can rule them out. You can promise a hundred times to waive it all, but it does not work that way. Again, I am speaking from experience. It does not work that way and some [9]

There is another way to handle it. The extreme way is to establish the estates in Israel. This of course means that the investors cannot pay less than minimum wage, (in any case, IPCRI believes that an Israeli industrialist cannot work in Gaza with paying less than minimum wage there while paying something else in Israel, at least this will be so after several years). We believe that there must be some way to balance the risks in the eyes of the investor. In other words, there must be means like insurance, and/or systematic mechanisms to build a system that takes into account the organizational and legal difficulties in advance. But even if there existed an agreement from the Israeli government to provide all the facilities necessary at this point, it would not be enough. There is a need to convince the Israeli investors to invest there and with a system and laws that are so new, it will take more time. Even if everything in a system is perfect, it has not functioned so far and there is no tradition to refer to regarding the risks involved. For that purpose, there is need for much more than just a good law.

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[8] Prof. Ezra Sadan , October 1998 at an IPCRI sponsored Roundtable Meeting on the Future of the Border Industrial Estate concept.

[9] Ibid.

A year ago, during Ramadan 1997, the Israeli Federation of Chambers of Commerce hosted a delegation of some thirty Palestinian businessmen headed by Deputy Ministry of Industry, Adnan Samara. On the Israeli side there was a similar number of businessmen. All of them came in order to learn about investment possibilities in the Gaza Industrial Estate. The only question raised by most of them, and some of them were

framework.[10]

When everything is settled and all the obstacles have been removed and all of the regulations have been set and published, in order to get Israeli investors there will still be a need for some sort of guarantees. These not guarantees at the high political level, but guarantees to the small or medium corporation that is going to invest. Governments can supply instruments such as guarantees that are bankable.

Palestinians obviously do not think that putting the Palestinian industrial estates under Israel's legal framework is the solution. They claim that there has to be coordination between the two sides in finding solutions for all the problems facing each of the industrial states. There are practical solutions, but there has to be commitment from both sides to decide on these solutions.

provide Israeli investors with all the guarantees they would like in order to
[11] Palestinians further state

that there is a well-defined legal framework that deals effectively with issues such as the repatriation of capital which is, in Gaza, the same law that

[10] Mandy Barak, Director of International Relations at the Israeli Federation of Chambers of Commerce at IPCRI Roundtable Meeting, October 1998.

[11] Dr. Abdul Malik Al-Jaber, Director-General of the Palestinian Industrial Estates

Industrial Estates, October 1998.

existed in Israel until 1980. Furthermore, as stated by Dr. Amin Haddad at

need to do is deal with one institution. To the credit of the Palestinian National Authority, they understood the complexity of their image and of dealing with a third-world bureaucracy. That is why they gave it to a professional private-sector institution. The Gaza industrial estate is managed by the private sector. Our objective is to make money and to develop the industrial state. Your business is our business. If you do not come invest with us we will not have business. With regard to the issue of a legal framework, we have a new law which deals with industrial state investment, locating an industrial state, licensing requirements, repatriation rules, arbitration rules, every detail. The Palestinian Authority brought in the best international consultants who had seen hundreds of industrial states, hundreds of export-processing zones, hundreds of free zones, and told them we want the business-friendliest environment. We know our image is bad. We know that when you speak of Gaza and the West Bank you speak of Intifada, of shooting, of bombs, of fighting Israelis and Israeli soldiers. We

legal framework. There has been established a code of bylaws on the Palestinian side governing investment in the industrial zone. The incentive package put in the Palestinian investment law provides for waivers. The estate will be an export-processing zone where imports will be duty-free and exports will be duty-free. This is very well laid out in the law. If you want to sell to the local market you can sell up to twenty percent duty-free, also from your duty-free imports of raw materials and processed goods. If you go beyond twenty percent, then you have to pay the normal local tariffs.

PALESTINIAN INDUSTRIAL ESTATES ON BORDER ZONES WILL REQUIRE THE GOVERNMENT OF ISRAEL TO DRAFT SPECIAL ISRAELI LEGISLATION

1. Preliminary Summary

These notes show that if the Government of Israel favors the establishment of the industrial estates on the border and wants them to succeed in attracting investment, Israel must pass far-reaching special legislation.

Special legislation is required, in brief, for three reasons: (1) to clarify for investors, particularly for Israelis and foreigners, precisely what are the commitments which Israel is undertaking in the context of the agreement with the Palestinians regarding the estates; (2) to clarify where the internal responsibilities created by the agreement fall within the Israeli governmental bureaucracy; (3) to harmonize the obligations undertaken by Israel in the context of the agreement with the Palestinians on the industrial estates with Israeli laws and international agreements (particularly the

2. Clarification to Investors

Israeli investors cannot reasonably be expected to invest in Gaza or the West Bank without some form of reliable guarantee that their operations will not suffer from non-individual treatment by Israel with respect to matters under Israeli control. This is most clearly manifest in the need of investors for uninterrupted <u>access</u> to their facilities for their workers, management, and suppliers, and for access out of the estates to Israeli ports or the airport. No investor will invest his capital in a situation where he could be closed down overnight because of security matters having nothing to do with his own operation. Some form of mechanism must be created which will either clearly guarantee that Israel cannot limit access without an individualized court action (e.g., create a corridor through the closure), or at least provide for prompt, adequate, and effective compensation for any losses due to non-individual restrictions on access (e.g., create government-sponsored non-commercial risk insurance for investments in the industrial estates).

In either of the above cases, however, the Israeli undertakings must be set forth in law, and not simply in policy statements or agreements signed with the Palestinians. Such policy statements or agreements do not have legal force. They can be changed or simply not implemented without creating any legal recourse on the part of a damaged investor who relied upon them. Furthermore, investors can be expected to calculate that a change in the Israeli government would be very likely to compromise the reliability of guarantees made by the present government, unless such guarantees are set forth in law. It is much harder to change a law than to change a policy, and a law is enforceable by the courts whereas a political agreement or policy is not.

3. Internal Responsibilities

Israel is undertaking various responsibilities with regard to infrastructure, such as power, water, telecommunications, and roads (at least with regard to external access to the Industrial Estates). The internal responsibilities of the various ministries and agencies within the Israeli government regarding these responsibilities must be clearly set forth in law. Otherwise, the agreement to cooperate could be killed in the bureaucracy. Furthermore, it is possible that some private interests within Israel will oppose one or another of the consequences of the arrangements for cooperation and may take legal action or lobby against it. A special law would protect the agreement signed by the government from stalling out due to these problems.

4. Harmony with Other Laws and Agreements

industrial estates must be harmonized with Israeli law and international obligations. The most important area is in taxation. Israel does not have a double taxation treaty with the Palestinian Authority. This means that unless some special law is drafted to provide otherwise, the earnings of Israeli companies in the industrial estates will be taxed in Israel. Thus, the effect of the special tax holidays established in the industrial estates by the Palestinian Authority with World Bank assistance will be significantly undermined with regard to Israeli investors. This is particularly onerous since, even assuming no income tax will be paid to the Palestinian Authority by an Israeli investor in the industrial estates, the same Israeli investor will pay more taxes on his profits in the industrial estates than he would had he earned the same profits in Israel. This is because the tax incentives offered for investments in Israel under the Israeli Law for the Encouragement of Capital Investment will not apply to Israeli investments in the industrial estates unless some special law equalizes the incentive scheme. Finally, although Israeli law currently provides that no duties are levied on materials imported into Israel for direct re-export, it is not clear that this exemption from duties will apply to materials imported into Israel for export to the border industrial estates. A special law would clarify this point.

with the USA and the EU. There are potential problems if untaxed goods enter the Israeli market from the industrial estates and could then find their way into trade with Europe or America. This potential problem could be corrected through special understandings with the US and the EU. The US and the EU should agree to treat certificates of origin from the industrial estates under the Israel-US and Israel-EU free trade agreements.

5. <u>Conclusion</u>

For the reasons described above, a special law is needed if the border industrial estates are to become a viable means of encouraging investment in the Palestinian territories and creating jobs for Palestinians. A law is needed to transform the purely political obligations undertaken by Israel in talks with the Palestinians and Israel into a legal commitment which investors can understand and rely upon. A law is also needed to set forth where responsibilities lie within the Israeli government, and to harmonize the commitments undertaken by Israel with other laws and international agreements.

Industrial Parks in Territories Controlled by the Palestinian Authority

October 1998

Prof. Ezra Sadan

1. <u>Introduction</u>:

Following previous Reports prepared by Sadan-Lowental Ltd[12] and various other sources, is seems reasonable to suggest that a solution for the severe unemployment and urgent need for export-revenue in the Palestinian economy which is both expedient and durable must rely on two paralleling endeavors:

- an attempt to re-instate the Palestinian position in Israel's labor market, having been eroded by closures and an influx of "guest laborers" from the Far East and Eastern Europe;

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[12]This Report follows a series of research documents prepared by Sadan-Lowental Ltd including:

A recent position paper published under the title "Save the Union" in <u>Palestine-Israel Journal</u>, , Vol. IV No. 3-4, 1988.

A Report commissioned by Israel's Minister of Defense in 1990, reviewed, summarized and published in 1995 t for the <u>Practical Peacemaking in the Middle East: The Environment, Water, Refugees and Economic Cooperation and Development</u> , New York: Garald Publishers.

A Report commissioned by Israel's Ministry of Foreign Affairs in 1996-7, summarized and published in 1998 Sourcing Alliances and Open Market Transactions, Trade in Goods between Israel, Jordan and the Palestinian Pfeifer (eds.) <u>The Economic Ramifications of Peace in the Middle East, Research in Middle East Economics</u>, Volume 3, Harvard.

A Report commissioned by Israel's Ministry of Industry and Trade in 1997 regarding Industrial Parks at the Economic-Frontier.

- an effort to develop domestic industrial and farming enterprises specializing in tradables.

Regarding re-instatement it may lead to a recuperation of the volume of employment enjoyed by Palestinians prior to the terror outburst in 1993, following the Oslo agreement. It is unlikely to remove the "guest-laborers" altogether and accord the Palestinians the benefits of Israel's growing labor market, since 1993.

Under these circumstances any solution of the severe unemployment and shortage of export-revenues in the Palestinian economy relies to a considerable extent on industrial development specifically designed to create jobs for Palestinians in the manufacturing of tradables. A policy of industrialization could be expedited should Israel play the role of either one of the following:

- a consumer market of final destination - for instance, the case of injected shoes produced in Nablus;

- a producer market of final destination - for example, the case of farm implements produced in Jenin;

- a gateway ushering Palestinian value added to the lucrative markets in the industrialized West - for instance, cut-flowers produced in Gaza and processed, forwarded and marketed by Israeli enterprises;

- a market for intermediary components outsourced by Israel's (exporting) industries - for example, packing, warping and encasing items made of paper, wood, plastic or metal produced by Palestinians and employed Israel's exporting industries.

Israel could be a gateway or a final destination for the Palestinian finished and intermediary goods should the respective **economic frontiers** be **penetrable**. Realization of the apparent market opportunities and taking advantage of the readily available marketing channels could be accelerated through the establishment of industrial parks along these frontiers.

Industrial parks established on the Palestinian side of the economically penetrable frontiers appear realistic for several reasons.

- With regards to the ever-impending security complications, parks established on the Palestinian side provide a closure-proof solution.

- Focusing investment efforts on particular industrial parks allow for the evolvement of industrial enterprises in spite of the insufficiencies of the physical infrastructure.

- Environment on the Palestinian side should be conducive to the formation of balanced entrepreneurial nuclei and management corps.

- Joint ventures on the Palestinian side would qualify for public international assistance and finance.

However, the establishment of parks and the encouragement of joint ventures on the Palestinian side of the frontier face certain difficulties in the underlying institutional framework.

- In essence, the composite structure of a written law, oral tradition and recorded experience intended to warrant personal and property rights - is lacking.

- Also, the legal and traditional foundation for entering into contractual entrepreneurial relationships and the settling of disputes - is deficient.

- In addition, the rules of origin regarding the cumulated (Palestinian-Israeli) values added remain unsettled.

2. <u>Action Required - the Palestinian Authority</u>

Interviews with potential investors in industrial parks on the Palestinian side of the frontier reveal one single major concern. Would-be investors are concerned with the legal framework[13]. In their mind the framework suffers from:

- incomplete legislation;
- deficient litigation and mediation procedures, and
- ineffective facilities to enforce compliance.

The Palestinian Authority should take action to adopt a modern[14] framework which guarantees the investors individual and property rights, allows for the free movement of capital and facilitates the conduct of present-day business enterprises. In particular, there is a need to develop the legal framework, which underlies commercial contracts - defining rights and obligations and providing accessible and "friendly" procedures for litigation and mitigation of disputes.

The Palestinian Authority should take action to develop a judicial system capable of handling corporate and individual (civil) controversies, labor disputes etc. At the same time, action should be taken to develop an effective facility to enforce compliance.[15]

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[13] IPCRI conducted a structured series of interviews for the World Bank in 1995. Among the non-Palestinian interviewed over 90% indicated three most important factors affecting their decision:
a framework which upholds property rights;
a framework which guarantees free movement of capital, and
the stability of that legal framework.
Discussions conducted in mid-1998 with potential Israeli investors in Palestinian "Industrial Estates" reconfirm IPCRI's early conclusion regarding the investors main concern.

[14] At this stage the Palestinian legislation in question relies on the Jordanian Procedure of 1953 and the Ottoman Law of 1827.

[15] As of today, outside entrepreneurs - including would-be investors - complain that debt collection in the Palestinian territory is practically impossible.

Legislation and the generation of the needed judicial and executive bodies are time consuming, the establishment of tradition and trust takes ages. In the meanwhile the Palestinian Authority should allow their system to accommodate outside (foreign) substitutes. For example, the system could uphold outside (foreign) mediation procedures adopted in contracts involving joint ventures between the Authority and Palestinian corporations on the one hand, and outside investors on the other[16].

3. <u>Action Required - the Government of Israel</u>

In order to encourage Israeli and foreign investors in frontier industrial parks located outside the jurisdiction of the State of Israel, the Government of Israel could consider the following political and economic measures:

- a guarantee of free movement of manpower, raw materials, intermediary and finished goods between Israel and the Parks;

- foreign investment insurance, within the framework of Israel's Foreign Trade Risk Insurance, and perhaps

- direct subsidies within the framework of Israel's Incentives for Industrial Investments.

Free movement of Raw Materials, Intermediary and Finished Goods - Fiscal Considerations:

In principle, free movement is guaranteed within the quasi-Custom Union agreed upon between the Israelis and the Palestinians in the Paris Protocol. Should a genuine and permanent Custom Union replace that Protocol, the question of free movement to and from the frontier parks is

[16] In principle, contracts could invoke the Israeli legal framework or resort to procedures prevailing in London or Washington D.C.

resolved. Otherwise, the functioning of the Parks will depend upon a particular guarantee of free movement provided by the Government of Israel.

(1) Free movement of Raw Materials, Intermediary and Finished Goods - Security Considerations: Security considerations hamper the free movement of goods. In Gaza, for example, security arrangements require a back-to back unpacking and re-packing of goods entering Israel with the intention to avoid the smuggling of explosive contraptions. The friction associated with these security arrangements is liable to interfere with the ordinary routines of production forwarding and marketing. There is a need to arrive at the "least-friction" (the closest to a frictionless) arrangement. The Government of Israel could contribute to that goal through investments in the security check-up facilities. (Needless to say that the Palestinian parks should be properly positioned and interconnected, to take full advantage of these facilities.)

(2) Foreign Investment Insurance - Investment in frontier parks on the Palestinian side, involve security, political and commercial risks. Security risks are associated with the outbursts of terror characterizing the particular environment. Political risks reflect the unique systemic deficiencies contemplated above and the instability typical of the young and inexperienced Palestinian administration. In contrast, commercial risk is supposedly a universal phenomenon. But, in the case in question these risks reflect the volatility of the system as whole. For example, where political and business affairs are intertwined (at the micro level) commercial risk is directly and indirectly associated with political risk. Under these circumstances insurance of political risk such as the one provided by the Government's insurance facility to investors in Jordan will not suffice. For investments in the Palestinian parks there seems to be a need for an all-risk insurance policy.

(3) Direct Subsidies - One way for the Government of Israel to provide direct incentives to investors in the Palestinian industrial parks is to allow for a "bankable" all-risk insurance policy which could be utilized by the investor as a collateral.

Another way to provide direct incentives to Israeli investors is to cover investments in the industrial parks **on either side of the frontier** under the law providing for incentives for industrial investments in Israel's periphery[17].

4. Action Required Common - the Government of Israel and the Palestinian Authority

As indicated above the authorities in charge of the frontier joint venture development should resolve the problem of the rules of origin.

Israeli industrialists export their products to the US and the EC and various other countries under free trade agreements. That status has been extended by the US to include Israeli-Jordanian products originating in the industrial zone in Irbid. In other words the relevant "rules of origin" were re-interpreted to consider the cumulated Jordanian and Israeli values added as if they were an Israeli value added. A similar arrangement with the US **and the EC** will be necessary to encourage Israeli industrialists to move into Parks located in the Palestinian territories.

Should a permanent Custom Union replace the Paris Protocol, the question of origin could be resolved through a sweeping international recognition of that Union. Otherwise, the functioning of the Parks will depend upon tripartite agreements regarding cumulation[18].

[17]In principle, that law covers investments on the Israeli side of various frontier locations, for example, the Israeli side on the outskirts of Gaza.

[18]It should be noticed that Israel is unlikely to accept agreements which distinguish between Palestinian parks, and parks developed by Jewish settlers in their vicinity.

During the last half of 1998 IPCRI conducted a survey amongst some 100 Israeli companies from four branches of industry: construction materials, plastics, textiles, and food processing. All of the companies selected for the survey currently have at least 50 employees and exhibited substantial enough profits to consider new investments. All of the industries concerned are labor intensive industries who draw mainly on Palestinian workers in their factories.

IPCRI used a modified version of the survey it developed for use in the World Bank survey it conducted in May 1995, both because it was a good survey and because it would allow us to compare results with similar work conducted then. The IPCRI survey was also used by the Israeli 1997.

All in all, IPCRI received 72 100 companies solicited. The results of the IPCRI survey highlight the same concerns found in 1995 by IPCRI in the World Bank study and by the Is 1997. The main findings in this latest survey are more explicit than in the previous surveys, in addition to the fact that all of the parties had already conducted a site visit to the GIE and had participated in at least one workshop attended by Palestinian officials and staff of PADICO to provide answers to their questions.

The survey questionnaire aimed at identifying the primary concerns of the potential investors. The issues investigated included (and rated by priority by the respondents) were:

1. The legal framework
2. Infrastructure
3. Manpower
4. Administration
5. Export possibilities
6. Incentives
7. Financing

Within the issue of the legal framework, the following items received a 99-100% response regarding the importance of the issue in making a positive decision to invest:

1. The ease of receiving licenses and permits
2. The mechanisms for guaranteeing court decisions
3. The preference of being able to utilize Israeli courts and the Israeli legal regime

On a scale of 1-5, 5 being the most important, the highest mean ratings given were for the following variables:

1. Political and security risks	4.4
2. Having enough and reliable electricity	4.5
4. Mechanisms and realization of agreements and court decisions	4.6
4. Modern legal framework	4.6
5. Ability to bring law suits to Israeli courts	4.5
6. Free passage of workers and goods	4.4
7. Telecommunications	4.3
8. Protection of trade marks and intellectual property	4.1

A brief analysis of each points teaches us the following:

1. Political Insurance

In order to significantly reduce the risks for Israeli investors, the government of Israel should facilitate the allowance for policies from the Israeli Foreign Trade Risks Insurance Company (IFTRIC) to be granted for use in the Palestinian areas. These policies must be bankable, e.g. transferable into loans and credit. It is possible and recommended by IPCRI to arrange for joint venture insurance policies with MIGA from the World Bank and OPIC from the United States, thereby reducing the direct risks to Israel and adding more insurance to the general available amounts for more investment.

2. The Legal Framework

The potential Israeli investors clearly indicated the importance for them of being able to settle disputes in Israeli courts. Some potential investors (46%) indicated a willingness to allow for arbitration to be used if implemented by accepted international standards (UNICTRAL Rules) and if the implementation of the arbitration can be guaranteed to be fulfilled. Most of the potential investors (88%) did not believe that either courts decisions nor the results of arbitration could be enforced in the Palestinian territories given their knowledge of the present legal regime.

Furthermore, Israeli companies with registered patents and trademarks or other elements of registered intellectual property registered in Israel do not wish to have to undertake a similar registration process in the PA.

3. Licensing

Most of the Israeli potential investors (68%) voiced concern that the process of licensing would be tedious and would require under-the-table payments. An additional concern voiced (72%) was with regard to the need to have ruling control of shares in any new company in the Palestinian territories. The current company law in Gaza does allow for 100% ownership of companies by foreigners (including Israelis), however the current company law in the West Bank only allows for a maximum of 49% holdings by non-Palestinians. There is concern that any new company law in Gaza would adopt the existing West Bank model rather than a more liberal model allowing for full ownership by a foreigner. In separate interviews conducted by IPCRI with potential investors, we found concern that even though the Gaza company law allows for 100% Israeli ownership, in practice it is nearly impossible to register a company in Gaza as an Israeli held company.

4. Free Passage and Free Movement of Goods

The survey shows that this is an essential element for investment in the Palestinian territories. The Israeli investors address the Israeli officials on this matter and not the Palestinian Authority. Most Israeli investors (92%) stated categorically that without guarantees from the Israeli side for free movement for their management, raw materials and finished products they would not invest in the Palestinian areas.

5. Taxation

Currently there is no treaty on avoidance of double taxation and the prevention of tax evasion. There is concern amongst the potential investors that they will be unfairly taxed by Israel due to the lack of mechanisms recognizing the tax incentives provided by the PA thereby reducing the incentives of investing in the Palestinian areas. The solution offered is for Israel to provide the investors with full tax credits so that when paying their taxes in Israel it will be as if they were paid in full in the PA and then this will be deducted from their taxes due in Israel. This is referred to as tax sparring which is used in many bilateral tax treaties.

6. Cumulation of Origin

In the current state of affairs there is no recognized cumulation of origin with regard to joint Palestinian Israeli ventures in the Palestinian areas vis a vis the European Union. This is also a matter of great concern to Israeli potential investors. More than two-thirds of those surveyed (67%) said that this is a crucial matter because they would expect their goods produced in the Palestinian Industrial estates to be exported mainly to Europe.

7. Export to the Arab World

Many of the surveyed potential investors (58%) stated that one of the incentives for them in looking into the Palestinian industrial estates was the possibility of being able to export to Arab markets that have not been exploited by them in the past.

8. Manpower

This too is a crucial issue but of less concern because most of those surveyed have positive experience with Palestinian laborers who according to them are well trained and have a high level of productivity.

Conclusions and Recommendations of the Survey

Addressing the legal regime issues should be given the highest priority as it is likely to be the main reason why investments do not become realized. Most Israeli potential investors realize that there are real advantages to working in the Palestinian areas. These reasons are not necessarily related to the incentives provided by the PA but rather due to proximity and familiarity. As it currently stands, there is no need for visas or passport controls or travel fees. Insurance for vehicles can be issued in Israel. There are no customs or other tariffs. The Palestinian laborers are more skilled than those in Jordan and Egypt and have a high productivity rate. Costs of communication is cheaper than communication with Jordan and Egypt. Managers can easily travel to the factories and return home every day saving costs on hotels and travel expenses.

include:

1. Political risk against upheavals, disturbances, closures, etc. (Israel, PA)
2. Insurance from Israel? Mixed packages with MIGA and OPIC, etc. (Israel, World Bank, US Government)
3. The PA should seriously investigate possibilities for resolution of disputes in recognized international or Israeli for a and provide answers for the enforcement of court and arbitration decisions. (PA and Israel)
4. Double taxation treaties (PA and Israel)
5. Revised company law (PA)
6. Credit (PA banks and Israeli banks)
7. Rules of Origin (EU)
8. Export to Arab countries (PA, PADICO, etc.)

Annex I

PALESTINE AUTHORITY
LAW ON THE ENCOURAGEMENT OF INVESTMENT

Law No. ( ) of 1995
Concerning the Promotion of Investment

The Chairman of the Executive Committee of the Palestine Liberation Organization President of the Palestinian National Authority.

Having the approval of the Council of the Authority, dated 29 April 1995. In accordance with the requirements of public interest. Hereby promotes the following Act:

Part I
Definitions

Article I
In this law, the following words and expressions shall have the meanings shown below, unless the context otherwise requires:

The Authority: The Palestinian National Authority.
The Agency: The Palestinian Higher Agency for the Encouragement of Investment.
Investor: Any natural or legal person seeking or offering to invest in Palestine.
Investment: Creation or addition of economic (production, industrial tourist, agricultural, medical, educational, productive, construction services) in Palestine, including :

* A.(Establishing new projects)
* B. (Expansion of Production lines, and adding new equipment and machinery designed to enhance productivity and create additional work opportunities.)

Dues: Customs duties and purchase tax levied on machinery, equipment, and raw materials Income Tax: Income tax levied on the net profit of investment projects.

Part II
The Palestinian Higher Agency for the Promotion of Investment

Article 2

1

this Law. It shall be an autonomous body corporate and shall report directly to the President of the Authority. The headquarters of the Agency shall temporarily be located in the city of Gaza, and its Board of Directors may establish branches or offices in side or outside Palestine.

2. (The Agency shall be concerned with encouragement of investment so as to ensure implementation of the Palestinian development needs in accordance with the objectives, priorities, and policies set by the Board.

Article 3

The Agency shall be managed by a Board of Directors composed of fifteen members under the chairmanship of the Minister of Economy and Trade - Industry.

Membership shall consist of following :

1. General Director of the Agency
2. A representative of the Ministry of Finance
3. A representative of the Ministry of Planning and International Cooperation
4. A representative of the Ministry of Industry
5. A representative of the Ministry of Public Works
6. A representative of the Ministry of Housing
7. A representative of the Minster of Local Government
8. The Governor of the Palestinian Monetary Agency
9. The Presidents of both the Federation of Chambers of Commerce and Industry
10. Four members from the private sector, who shall be appointed by

decision of the President of the National Authority

11. A representative of the concerned Ministry, depending on the project(s) proposed

* Other ministries and agencies shall be represented by undersecretaries or general directors. Membership shall be for a renewable term of three years. If the seat of a member of the Board of Directors falls vacant, whoever has the right to appoint such a member shall appoint a substitute for the remainder of the term of membership.

* The Agency shall be chaired by the representative of the Ministry of

Article 4
The Agency shall have the following powers and functions:

1. To direct investments according to the approved priorities and policies based on the Palestinian economic need and in cooperation with the Ministry of Economy and Trade-Industry, and other concerned ministries.

2. To formulate and develop information packages to inform the Investor about available opportunities and to promote such opportunities by various mass media.

3. To formulate suggestions and to improve and develop this law when necessary.

4. To collect, coordinate, and publish studies on the encouragement of local, Arab and foreign capital investment in various projects, and to contact agencies for the promotion of investment.

5. To hold economic conferences and invite Palestinian, Arab and foreign investors participate.

Article 5
The Board of Directors shall have all the powers to conduct the business of the Agency and to formulate its general policy in a manner consistent with the objectives and functions provided for in this Law.

Article 6
a) Decisions of the Board of Directors shall be adopted by a majority vote of those present. The Chairman shall have the deciding vote in the case of a tie. The quorum of the Board's meeting shall be the presence of two-thirds of the number of members.

b) The Board of Directors shall meet at least once a month whenever so required at the convocation the Chairman, or at the request of one-third of the members.

c) The Chairman or any other member of the Board of Directors shall not participate in any decisions related directly or indirectly to the interests of that member.

d) The Board of Directors may invite any person, without having the right to vote, to attend its meetings if there is a need to render an interpretation or consultation.

Article 7
The Agency shall have Director-General, who shall be appointed by
s president.

Article 8
The Agency shall have an annual budget with revenues derived from :

1. Contributions from the Palestinian National Authority,
2. Service fees as determined by the Board of Directors, and
3. Donations and grants that do not contradict public interest.

Article 9
The Agency Board of Directors shall appoint auditors to audit the accounts in conformity with generally accepted practices and submit a financial report to the President of the Authority every six months.

PART III
Development Areas and Sectors

Article 10

1. The development areas under the jurisdiction of the Palestinian National Authority shall be divided into two regions, (A), (B), and (C), depending on their nature and relevant economic policies. The Agency shall designate and announce these regions pursuant to a decree to be published in the official Gazette.

2

aforementioned development regions and specify appropriate incentives for each region. The investor will have the right to object to the decision, and this shall not apply to enterprises that have already been approved.

3

specific economic investments required to promote the interests of the Palestinian national economy.

PART IV
Exemptions

Article 11

1. Projects which are approved by the Agency and which have obtained the requisite licenses in accordance with the applicable laws shall be granted the exemptions for under this law in conformity with the following criteria:

Category (A) : A project with paid-up capital of more than five hundred thousand US dollars (500,000) or which permanently employs no fewer than 25 Palestinian workers shall be granted an exemption from income taxes, when they fall due, payable and from duties for a period of five years, provided that the life of the economic project is not less that ten years.

Category (B) : A project with paid-up capital of more than one hundred and fifty thousand US dollars ($150,000) , or which permanently employs no fewer than 15 Palestinian workers shall be granted an exemption from income taxes when they fall due, and from duties for a period of three years, provided that the3 life of the economic project is not less than six years.

Category (C) : A project with paid-up capital of more than one hundred thousand US dollars ($100,000) or which permanently employs no fewer than ten Palestinian workers shall be granted an exemption from income taxes when they fall, and from duties for a period of two years, provided that the life of the economic project is not less than five years.

exceptional exemptions to a project with a paid-up capital of more than five million dollars ($5,000,000) and which employs no fewer than fifty permanent Palestinian workers.

2
exemptions depending on the nature of the project and the needs and development priorities of the Palestinians.

Article 12

to export projects, providing that percentage of output processed for export is not less than 25 per cent of the total output and that the value is not less than 30 per cent of the total cost of the project. The Board of directors may also consider granting additional incentives for export-oriented agricultural projects.

PART V
Exemption Procedures

Article 13
1. To benefit from the exemptions provided for under this law, an investor shall submit an application supported by a technical and economic feasibility study of the project and shall satisfy all licensing procedures or any other requirements provided for under applicable laws and regulations.

2. The Agency shall, within thirty to sixty days from the date of application, notify the applicant of its approval or rejection and shall state the reasons there of.

3. In the event of the approval of the exemptions, the investor shall submit an action plan detailing the steps to be followed to complete the project provided that the project implementation start-up period shall not exceed six months from the date of approval.

4. The investor shall submit to the Agency information and data required

designate officials(s) to conduct field trips to verify the information presented.

Article 14
The exemption procedures provided for in this Law shall apply to all areas of investment except the following sectors and areas which require prior approval by the National Authority:

The manufacture and distribution of weapons, ammunition, or their parts;

* the aviation industries, including airports,
* the electrical power generation and distribution,
* the reprocessing of refuse and solid waste, and
* telecommunications services, including radio and television.

Article 15
Upon any transfer of ownership, the project shall continue to enjoy the same exemptions previously granted, providing that it continues to be operated in the same manner by the new owner and who adheres to the provisions of this Law.

Article 16
A project owner who benefits from the provisions of this Law may sell his exempted fixed assets to another project enjoying the same privileges under the provision of this Law, provided that the Agency approves such a sale, giving priority in the purchase of these assets to Palestinian investors.

Article 17
The Agency shall publish a list of all approved projects in the Official Gazette every six moths, giving a brief description of such projects.

PART VI
Guarantees Against Nationalization

Article 18

1

nationalized, confiscated, or expropriated in whole or in part without the

except in compliance with a final judgment handed down by a competent court.

2. Foreign, Arab, and expatriate Palestinian investors shall enjoy the same rights and privileges as those granted to local Palestinian investors.

3. Expatriate Palestinian investors, as well as Arab and foreign investors, shall enjoy the right of permanent residence in accordance with applicable laws.

4. An investor, having paid the dues provided for under the applicable laws, may repatriate the capital in accordance with the provisions of this law.

5. Foreign, Arab, and expatriate Palestinian investors may repatriate the capital and profits generated from investments approved under this law, after payment of the dues provided for.

PART VII
Suspension and Cancellation

Article 19

1. Should the Agency find an investor who has been granted a license who has failed to comply with the provisions of this Law or its regulations, or who has failed to abide by the conditions specified in the investment license, the Agency shall notify the investor in writing of its intention to cancel or suspend the licensed exemptions on the future or retroactively.

2. Should the Agency find that the license was granted to the investor under false pretense, deceit, bribery, or forgery, or in a manner contrary to this law and its regulations , the Agency may revoke such a license as of the date of its issue. All taxes, duties, and other benefits and privileges granted to the investor shall be deemed payable immediately, with interest accrued from the date the license was issued.

3. In either of the tow above mentioned occurrences, the investor may complain within thirty days from the date of notification of the decision, with the President to the Authority Chairman, whose decision shall be final.

PART VIII
Settlement of Disputes

Article 20

The Palestinian courts shall have the competence and jurisdiction to resolve all disputes in accordance with applicable Palestinian laws.

PART IX
General and Final Provisions

Article 21

1. All investments shall be effected in accordance with the license granted

to them, without any discrimination based on sex, race, or religion in employing local staff, procurement, or conducting any activity.

2. An investment may be made in any economic project, provided that it shall not conflict with public morals, public order, public security, and environmental protection laws.

Article 22
Any text contrary to the provisions of this Law shall be invalid and revoked.

Article 23
All competent authorities, within their respective areas of jurisdiction, shall execute this law, which shall enter into force from the date of its issuance and shall be published in the Official Gazette.

Issued in Gaza on 30/4/1995
Yasser Arafat
Chairman of the Executive Committee of the Palestine Liberation Organization
President of the Palestinian National Authority

PALESTINE LIBERATION ORGANIZATION

PALESTINE NATIONAL AUTHORITY

Office of the President

LAW NO. (10) FOR YEAR 1998
FREE INDUSTRIAL CITIES AND ZONES

Chairman of the Palestine Liberation Organization Executive Committee
President of the Palestine National Authority

Upon a proposal by the Minister of Industry
Based on the needs of the public Interest
And after reviewing the project presented by the Cabinet
And after the approval of the Palestinian Legislative Council in its session held on / / .

The following law was issued:

Chapter One

Definitions and General Provisions

Article (1)

In implementing the provisions of this law, the following terms and expressions will have the following definitions unless otherwise stated:-

Minister: Minister of industry.
Ministry: Ministry of Industry.

The Commission: The general commission of industrial cities and free industrial zones.
The Board of Directors: The board of directors of the commission.
The Applicant: Any person or institution qualified according to regulations and charters to submit an application according to this law to allocate a region in

Industrial City: A specific geographical region established according to this law, allocated to serve a number of beneficiaries to implement industrial activities and services; the region will have special privileges granted by this law.

Free Industrial Zone: A specific geographical region established according to this law allocated to serve one beneficiary or more in order to implement export activities; the region will be subject to special provisions pertaining to customs and taxes granted by this law.

Manufacturing Project: Any project licensed to work within an industrial city and which manufactures a new product through transforming organic or/and inorganic substances into new products by changing their size, shape, nature or quality, using manual or mechanic devices, or through assembling parts so that they become another product, including packaging products.

Licensed Project: Any manufacturing project licensed to work inside the free industrial zone.
Certificate of Free Industrial Zone: A certificate issued by the commission according to the provisions of this law stipulating that a licensed project has the right to begin operating in a free industrial zone.

The Developer: The qualified party with which a contract of privilege is signed according to this law for purposes of developing and managing an industrial city.

Contract of Privilege: The agreement made between the developer and the commission in order to establish or develop and manage an industrial city and/or a free industrial zone.

Decision of Allocation: The decision taken by the Cabinet according to this law concerning allocating an industrial city and/or free industrial zone in Palestine.

The Investment Window: The commission or any of its offices that are located within the borders of the industrial city and/or the free industrial zone through which the investor can get all permits, licenses and official registration needed for his project.

Article (2)

According to the provisions of this law, a commission to be named

will be established in Palestine with an independent artificial character, enjoying legal status that grants its rights in achieving its purposes and in exercising its activities according to the provisions of this law.

Article (3)

The Commission will be considered the Investment Window in the industrial cities and free industrial zones.

Article (4)

The main headquarters of the commission will be in Jerusalem while the temporary headquarters will be in any place decided upon by the National Authority; the commission has the right to open branches anywhere in Palestine.

Chapter Two

Goals and Tasks of the Commission

Article (5)

The Commission will have the following tasks:

1- To set up a general comprehensive policy to establish and develop industrial cities and free industrial zones in Palestine.

2- To submit proposals, plans and recommendations to the Cabinet concerning establishing, developing and managing any industrial city or free industrial zone in Palestine.
3- To accept and receive applications pertaining to establishing industrial cities and free industrial zones for purposes of establishing industrial projects and submitting them with recommendations to the Cabinet.
4-To look into applications submitted by various parties concerning licenses to work in an industrial city and/or a free industrial zone; in addition, the commission will grant free industrial zone certificates to investors.
5- To develop industrial cities and free industrial zones, either directly or through developers.
6- To prepare plans and programs pertaining to the development of industrial cities and free industrial zones.
7- To establish public facilities required by industrial cities and free industrial zones or to allow others to establish them.
8- To determine the fees for services to be provided by the commission for the industrial cities and free industrial zones and the basis of their collection according to law .
9- To make agreements and contracts and accept assistance and donations that are offered in a way that does not contradict with the provisions of this law.
10- To ratify the annual general budget of the commission and submit it to the competent parties to be ratified according to standards.
11- To choose developers and sign contracts with them.
12- To monitor the performance and development of industrial cities and free industrial zones and publish the relevant reports.
13- To work towards implementing local and regional agreements pertaining to any matter mentioned in this law.

Chapter Three

Board of Directors

Article (6)

A- The Commission will have a board of directors consisting of 11 members in the following manner:

1- Minister of Industry	President
2- Representative for each of the following:	
a- Ministry of Economy and Trade	Vice-President
b- Ministry of Finance	Secretary
c- Ministry of Industry	Member
d- Ministry of Planning and International Cooperation	Member
e- Ministry of Local Government	Member
f- Ministry of State for Environment Affairs	Member

3- Four representatives, two from the developers and two f
rom chambers of commerce and industry, and industry unions.

B- The representatives from developers, chambers of commerce and industry and industry unions will be nominated by their competent parties; a decision from the President of the National Authority will be issued to appoint the members of the board of directors upon nomination from the Cabinet.

Article (7)

The membership in the board of directors of representatives of developers, chambers of commerce and industry and industry unions will continue for a period of two years, after which nominations will be made to replace them; the commissions have the right to re-nominate members whose membership was terminated provided that members will retain their positions on the board until another person is nominated in his place.

Article (8)

Any member convicted for offenses related to honor or honesty or whoever declares bankruptcy or is convicted of an offense according to the company laws in effect will lose membership in the board.

Article (9)

Members of the Board of Directors and workers in the commission must maintain confidentiality in carrying out their work.

Article (10)

In order to achieve the goals and tasks of the commission, the board of directors shall assume the following jurisdictions:

1- To ratify the working plan adopted by the commission in the context of a general policy set for it.
2- To supervise the lands of the industrial cities and free industrial zones and the parties working there, in addition to publishing periodical reports to this effect.
3- To organize local and international propaganda campaigns to promote industrial cities and free industrial zones in order to increase investments and cooperation with competent parties on this issue.
4- To set up charters organizing the work of the commission inside the industrial cities and free industrial zones pertaining to financial, administrative and technical aspects.
5- To nominate the general manager of the commission.
6- To formulate a general policy regarding the employment of workers in the commission and to decide on the scale for their salaries.
7- To approve the employment of experts and advisors.
8- To issue various debt instruments within the general conditions applicable according to the law.
9- To issue the necessary decisions pertaining to the tasks of the commission.

Article (11)

A- The commission will have a director-general who is appointed by a decision from the Cabinet upon nomination from the board of directors.
B- The director-general will participate in the board of directors meetings and in all discussions without the right to vote.
C- The director-general is to be considered the executive official in the commission with the following tasks:

1- To implement the commission policies as outlined by the board of directors.
2- To organize and supervise the daily operations of the commission.
3- To submit reports to the board of directors on a regular basis regarding the operations and performance of the commission.
4
Palestine and abroad.

D- The salary and other financial rights of the director-general are decided upon by a decision from the board of directors.
E- The director-general cannot be part and should not have any direct or indirect interest in any manufacturing project, any licensed project or any contract signed by the commission.

Article (12)

The board of directors has the right to commission the director-general of the commission with some of its tasks and has the right to seek assistance of any specialized committee or other experts.

Article (13)

The board of directors meets at least once every month upon a request by the President of the board, or his deputy in case of his absence. The meeting is considered official if is attended by a two-third majority of members, including the president or the vice president. Board decisions are taken upon the approval of the majority of members attending; when votes are equal, the side supported by the president wins; the board can be called for an urgent meeting upon a request by the director-general after the approval of the president of the board.

Article (14)

If there is any personal benefit, direct or indirect, of any member in the board of directors concerning any application submitted to the commission by a qualified person or a developer to allocate an industrial city and/or a free industrial zone or to develop or license any project in it, the member should declare this in writing to the board and will have no right to participate in any decision or recommendation issued by the commission concerning that application.

Chapter Four

Finance

Article (15)

The financial resources of the commission consist of the following:-

1- Funds allocated to the commission from the general budget of the National Authority.

2- Fees collected from granting licenses for industrial cities and/or free industrial zones.

3- Fines collected according to the provisions of the law.

4- The grants and loans offered by countries, international organizations and international and local NGOs.

5- Any other revenues collected according to the provisions of this law.

Article (16)

All incomes and revenues of the commission are deposited in a special account in the treasury account to be placed under the supervision of the finance ministry; a special budget will be allocated to the commission within the annual general budget of the National Authority; all expenses of the commission will be from this account.

Article (17)

In organizing its accounts and records, the commission will follow the standards and principles of international accounting; the board of directors will appoint a certified auditor to audit the accounts and records of the commission.

Chapter Five

Establishing Industrial Cities and Free industrial Zones

Article (18)

The commission has the right to recommend to the Cabinet, either directly or through a submitted application, to issue a decision to allocate any appropriate location in Palestine to become an industrial city and/or a free industrial zone; if the lands where the industrial cities or the free industrial zones are established are rented, the lease period must not exceed 49 years.

Annex III

Re-evaluating the Border Industrial Zones Concept

IPCRI was one of the first organizations to propose the establishment of border industrial zones between Israel and the Palestinian Authority. On the basis of a paper written several years ago by IPCRI, Prime Minister Yitzhak Rabin created a inter-ministerial committee to investigate the possibilities for such a project. The IPCRI paper looked at three models for border industrial zones:

1. A zone located on the Israeli side of the border completely under Israeli legal jurisdiction
2. A zone located on the Palestinian side of the border completely under Palestinian jurisdiction
3. A cross-border zone located in both Israeli and Palestinian territory under some form of joint jurisdiction

IPCRI paper clearly presented a case for the third option, but because the Palestinians clearly preferred the second option and the Israelis really the second option was selected. Today, after millions of dollars spent, the Gaza Industrial Estate remains virtually empty.

IPCRI had conducted a pre-feasibility study for the World Bank investigating potential for investment in the Gaza zone. The findings of that study were published in a World Bank study. During the past year, IPCRI conducted an additional study evaluating whether or not Israeli firms would set up factories in the Gaza Industrial Estate. Our findings together with a study that we contracted from Prof. Ezra Sadan from Sadan-Lowenthal composes the contents of the proposal that we would like to request your support to produce. The study indicates the primary concerns of potential Israeli investors as well as analyzing the legal framework or the zone with clear recommendations for changes in the concept so that the Gaza Industrial estate will have a better chance for success.

Some Thoughts on the Creation of Employment in the Palestinian Territories

Transboundary Industrial Zones[19]

January 1995

Gershon Baskin, Ph.D.

1) Industrial Zones

The basis of this suggestion is that rather than bring the workers to the work, the work should be brought to the workers. There are many ways of conceptualizing this plan and of viewing its development. The following are several of the variables which much be considered:

a. Location
- i. On the Israeli side of the border
- ii. On the Palestinian side of the border
- ii. a transboundary zone

b. Ownership and management
- i. government
- ii. private sector
- ii. mixed private and public sector ownership and management

[19] The following is part of a memorandum drafted and sent to Prime Minister Yitzhak Rabin in January 1995. This memorandum led to the creation of a Ministerial Committee on Joint Industrial Zones.

c. Make-up of Factories in the Zone
    i. Israeli
    ii. Palestinian
    iii. Foreign
    iv. foreign and local joint ventures
    v. Israeli-Palestinian joint ventures

d. Incentives and who provides them
    i. Israeli
    ii. Palestinian
    iii. The World Bank

The Ideal Scenario

The ideal scenario of the industrial zone would be as follows:

The zone will be a transboundary zone, located both in Israeli sovereign territory as well as in the Palestinian territory. The ownership and management of the zone would be private but the governments would provide the basic infrastructures. Incentives would be provided by both governments as well as the World Bank. The World Bank would provide loans and grants for the construction of the infrastructure of the zones as well as providing capital grants and low interest loans for factory relocation.

all of the incentives relevant in this classification. This includes tax holidays, grants and other incentives. Exporting from the zone would be encouraged both for the local markets and for foreign exports. The make up of factories would be a combination of all the options listed above (Israeli, Palestinian, foreign and combinations of joint ventures).

The Reality

The real situation is unlikely to develop according to the model illustrated above. The various options and variables should be examined in order to determine their possible implications.

Location

The easiest and probably the fastest way of creating such industrial zones would be for Israel to take a unilateral decision and simply develop areas on the border of the green line near densely populated Palestinian areas. These zones would be Israeli. Israel would develop them as she sees fit. There could be private sector involvement and probably would, if Israel could encourage private companies to invest in the development of these zones. The ideal situation for Israel would be to tender out the ownership and/or the management of these zones. Labor intensive industries would be encouraged by Israel to move to the zones and perhaps Israel could convince some of the donor countries to contribute funds towards the relocation of factories as they will provide labor mainly to Palestinians. Israel could also try and encourage foreign investments in the zone, however, it is highly unlikely that these investments will find their way there because foreign labor intensive industries will most likely still prefer to locate in regions with greater political stability.

The primary potential problem with the above model is that the means of employment will be solely in the hands of Israeli interests and the laborers will be mainly Palestinian. Management and ownership will be Israeli and Palestinians will provide cheap labor. This is only a modified form of colonialism and would probably be successful only in the very short term. Eventually, it is likely that the industrial zone would turn into an arena of terrorism or sabotage which would drive industries out from the area. The Palestinian Authority would see little interest in squashing rejectionists of

economic investment in the zones.

The Palestinians could unilaterally create industrial zones near the borders on their side. They could try to attract Israeli factories to set up shop there, but this is highly unlikely to succeed unless there is a significant improvement in the political stability and in the security situation. Most Israeli factories would prefer, at this point, to find more expensive replacement workers than to move their operations to the Palestinian sectors. The Palestinians could also try to attract foreign investment, but this too is unlikely to succeed.

The other option, then, would be for Israel and the PNA to combine efforts and create a transboundary industrial zone (or zones) which would be located physically on lands from both territories. The conditions for operation of the zones would have to be carefully negotiated.

Some of the issues to take into account are:

1. Ownership of the zones - public or private
2. Taxation and tax revenues
3. Private-Public sector involvement in the construction and management of the zones
4. Who are the owners of the factories (Israelis, Palestinians, others)
5. What industries can be located in the zones
6. Risk insurance and other forms of insurance
7. Banking regulations

1. The question of ownership of the zone is crucial to determine how the zone develops and how it is perceived. In any event, it would seem essential for any project of this kind to be based on parity between the sides. If the public sector is to be involved, there must be parallel arrangements for both authorities. If the zone would be owned and/or managed by the private sector involving Israeli and Palestinian interests, the same would apply. Parity should be sought in this question. Outside, third parties could be brought in as investors in the project and in fact, this would probably strengthen the likelihood of the success of such a project. This issue should not be underestimated in its importance.

2. The question of taxation and revenues is also very important. Industrial development is very important to provide a tax basis for the PNA. Likewise, Israel is not interested in reducing its own tax basis. Arrangements will have to be made in order to guarantee a regular and consistent flow of taxes. While tax incentives may be provided for companies choosing to relocate or to be established in the zones, the income taxes for workers, VAT and possibly municipal (property) taxes will have to be paid. Mechanisms for this must be established within the framework of the negotiations on the zones. There are many possibilities for arranging this, e.g.:

a. splitting all tax revenues equally between the two authorities

b. Income tax revenues from Palestinian workers to the PNA and income tax revenues from Israeli workers to the Israeli authorities. Special arrangements could be made if there are workers who are neither Israeli nor Palestinian.

c. Municipal (property) revenues could also be split or they could be funneled into a special fund for the purpose of creating additional zones or for the encouragement of the development of the zone itself.

3. Private-Public sector involvement in the construction and management of the zones.

As stated above, parity is a key question. The most likely scenario if this concept is to take hold is that the public sector authorities will be the owners of the industrial zones. If this is not the case, it can probably be assumed that the public authorities will, at least, be the owners of the land upon which the zone is constructed. It would be wise for the public authorities to tender out the development, construction and the management of the zone. In this case, a joint venture involving an Israeli and a Palestinian company, with the possibility of a third party, could create a holding company or a development-industrial company which would construct and manage the zone. Factories choosing to locate within the zone would have to purchase or lease space and facilities from the holding or development company and not from the public sector authorities. The holding company would be free to raise capital in capital markets. The holding company could purchase services freely from private sector companies and/or from public companies (this question would have to be resolved in the negotiations on the establishment of the zones between the Israeli and Palestinian authorities. The question of what company provides electricity, water, waste disposal services, etc. is a crucial element within the negotiations).

4. Who are the owners of the factories (Israelis, Palestinians, others)

The make-up of the factories within the zone is also crucial to the long-term success of this concept. Initially, it would probably most likely and feasible to encourage existing Israeli factories to simply re-locate within the zones. These would most likely be labor-intensive industries in food processing, textiles, etc. This should be encouraged through a range of

possibility of the zones becoming mainly Israeli economic interests seeking low-wage Palestinian labor. This danger is already mentioned above.

The developers of this concept, must from the outset, encourage joint venture between Israeli and Palestinian companies which would receive incentives to locate within the zones. This is essential to the success of this zone in terms of insuring not only employment to the Palestinians, but sustainable economic development.

The developers in a later stage, once there is more political and economic stability, should actively seek out international investments which could be located within the zones. The more of an international character that will eventually develop to the zones, the greater the chances for long-term success and furthermore, long-term sustainable development.

5. What industries can be located in the zones

Eventually, the develops of the zones should provide preferences for industries which are mainly export oriented, however, initially, this should not be a matter for great concern. The first challenge must be to provide employment and the market for the goods produced should be of little concern. An issue of concern should be the environmental sustainability of the industries located within the zones. High environmental standards should be set from the outset and all factories should be made directly responsible for recycling and effective control of wastes. It is very important that the zone be clean and green. This will help to encourage future investments within the zones. These standards can only be set from the beginning. Pollution prevention is not only cheaper than pollution clean-up, it is also a wise policy to adopt to encourage additional investments in the future.

Security Within the Zone

The more of a joint nature that zone encompasses, the greater will be the security for all parties involved. Nonetheless, security is an issue which must be addressed both in negotiations and in the management of the zones. The normal security problems which exist for any factory anywhere (theft, vandalism, fire, etc) are only more complex and serious given the political situation in this region. Providing as near to absolute security is essential for this concept to succeed. The provision of security is costly and should probably not become the burden of the industries located within the zones. The expenditures for security will have to be covered by the public sector authorities (which may be able to get some support from international bodies to help off-set this costs).

Incentives

There are numerous incentives which could be provided in order to encourage private companies to locate within the zone. But, first, there are also potential incentives which could be provided to the authorities to encourage them to adopt this concept and to develop it. These are:

1. Greater economic stability in the Palestinian areas which would, in all likelihood, turn into greater political stability.

2. Potential capital grants and loans from donor countries

3. Creating a model of successful cooperative economic development which could be copied by others around the world

4. Increased foreign investment

5. Possibility of increased exports

In order to encourage companies to locate within the zone the following kind of incentives could be offered:

1. Tax holidays
2. Moving expenses
3. Capital grants and loans
4. Sharing of some marketing expenses
5

creation of joint ventures

It would be wise to encourage international bodies such as the World Bank to provide some of these incentives. The easiest incentives for the World Bank to provide could be the relocation expenses and capital grants and loans for the development and expansion of new businesses (incentives could be linked to the number of jobs which would be created. The more jobs created the greater the incentives given).

Additional incentives or more substantive incentives should and could be provided for the encouragement of all kinds of joint ventures: Israeli-Palestinian, Israeli-foreign, Palestinian-foreign and any other possible combinations.

Annex IV

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Dr. Gil Feiler, Director

10; Free Industrial Cities and Zones

Law No. (10) for Year 1998; Free Industrial Cities and Zones is very general and

main substance sets out the goals and tasks of the General Commission for Industrial Cities and Free Industrial Zones. The Law also outlines the financial regulations governing the Commission.

In my review of this Law, I would prefer to avoid being critical, but instead wish to make the reader aware of the strong competition that the Palestinian Authority faces in attracting foreign investment. When searching for a location in which to set up a manufacturing facility, foreign investors search for detailed investment laws governing the industrial zone. It is thus imperative that the Palestinian Authority establishes a set of investment laws that are open, transparent, and competitive with the laws in other regional countries. This is especially important, considering that so many other circumstances are unstable in the Palestinian Authority.

investment, presently has a wage rate roughly half of that in the West Bank and Gaza. Land is also cheaper in Jordan, and its infrastructure is more developed than in the Palestinian Authority. Furthermore, Jordan has more actively sought foreign investment, including joint ventures with Israel, than has the Palestinian Authority. ent laws have been modified to decrease, if not eliminate the possibility of political or other irrelevant criteria tainting the investment approval process. This alteration has instilled investor confidence in Jordan. PA Investment Law No. (10), however, only makes a vague reference to this issue, under Article (14). This provision states that members of the board of directors of the General

Commission shall not participate in any investment decision in which they have any direct or indirect personal benefit.

The Palestinian Authority must explicitly reform its investment approval process, far beyond what is contained in Investment Law No. (10), in order to guarantee to foreigners that political or other irrelevant criteria will not taint the process. The Palestinian Authority does possess sufficient autonomy over its own affairs to take the necessary action to better attract foreign investment and to compete with other

recent ability to implement policies and attitudes that are conducive to investment and economic development. Foreign investment in Egypt has increased noticeably in recent years, and its privatization program is proceeding at a steady pace. While the details of investment laws are significant, in the long run, the Palestinian

their practical actions, including joint ventures with Israel.

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Annex V

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(Translated from Hebrew)

To: IPCRI
Subject: The Gaza Industrial Estate

With regard to the Palestinian law for the Industrial Estates Zones, I would like to emphasize the following:

The proposed law is not a law that provides protection for investors, it is merely a general program for the management of the industrial estate. The foreign investor, including Israelis, need to know under what legal framework they are working and in what ways their investments are protected. We see no relation to these matters in the Palestinian law.

Another issue that is connected to the Palestinian industrial estates is the matter of rules of origin and cumulation of sources of origin. A factory which imports raw materials in Israel and then re-exports them in the form of a final product receives a return of the customs duties paid for the import, however, in the case of the Palestinian industrial estates it is still unclear how this process will work, if at all. This matter presents a major obstacle for the operation of the Palestinian industrial estates.

Yours Sincerely,

Mandy Barak
Director, International Division