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**ON STRENGTHENING THE EUROPEAN NEIGHBOURHOOD POLICY**

**ENP Progress Report**

**Israel**

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## Overall assessment

The EU-Israel ENP Action Plan was adopted on 11 April 2005. It sets out the joint ambition to develop closer relations as anticipated in the conclusions of the Essen Council of December 1994 which stated *inter alia* that: “The European Council considers that Israel, on account of its high level of economic development, should enjoy special status in its relations with the EU on the basis of reciprocity and common interest...” On that basis, the EU and Israel concluded an Association Agreement, and developed relations further in the context of the Euro-Mediterranean Partnership.

The Action Plan takes this process still further by setting out in more detail than the Association Agreement a comprehensive set of jointly developed priorities, with a programme over three years of specific activities to which both sides are committed. A set of ten sub-committees of the Association Agreement has been established, bringing together specialists on both sides to guide and oversee the implementation of the Action Plan. In the first year of implementing the Plan, the sub-committees decided to focus on a selected group of priorities, and set a timetable for their sequencing and implementation.

This document reports on progress made on the implementation of the priorities addressed in the first year. As such, it concentrates primarily on the development of EU-Israel bilateral relations, and on technical issues involved in implementing the Action Plan. It is not a general review of the political and economic situation in Israel. This was last set out by the Commission in the Country Report for Israel published in May 2004.

Nevertheless, it remains true that bilateral EU-Israel relations in the context of the ENP Action Plan cannot be thoroughly reported without reflecting the overall political situation in the Middle East. The period covered by this review witnessed a serious escalation of the conflict, involving military action in Lebanon, with a significant impact on the daily lives of the population in Lebanon, the Palestinian Territories, and Israel.

The EU’s view on some of these matters, where relevant to this technical report on progress with the Action Plan, is set out in summary in the section below on political dialogue and cooperation.

In general, implementing the Action Plan has begun to help better define the path and framework of the EU-Israel relations while enabling to deepen and strengthen the co-operation in a wide spectrum of areas. In the course of implementing the Action Plan, EU-Israel cooperation has developed further than ever before in the area of political dialogue, promoting trade and investment, justice and security, science and technology including space cooperation, as well as higher education.

During the initial period of the Action Plan, the EU has been more closely involved with Israel in the peace process, in particular through a number of specific actions designed to assist certain aspects of Israeli-Palestinian relations, including border facilitation, humanitarian and economic support to help stabilise the situation in the Palestinian Territories. There has been a greater understanding between the EU and Israel of each other’s position on a number of issues, and a greater convergence of views on dealing with terrorism, including Israel’s legitimate right of self-defence, and threats to regional stability. Despite this progress, differences remain on important questions relating to respect for international law and human rights in the context of the conflict, difficulties in respecting the principles of the

Roadmap, and a number of issues affecting the potential to reach a final status agreement between Israel and the Palestinians. These issues are the subject of continuing dialogue, including in the context of the Action Plan.

On a specific issue, the Action Plan states that in preparing its first review, the EC will undertake an overall examination of Community programmes and bodies with the objective of opening them to Israeli participation. The Commission has prepared a review and is presenting proposals to the Council and Parliament on this matter. From the set of Community Programmes entering into force from 2007 onwards for which the Commission proposes to open to ENP partner countries, Israel has expressed interest in participating *inter alia* in: the CIP (Competitiveness and Innovation Programme), Customs 2013, Fiscalis 2013, Marco Polo, Youth, MEDIA 2007, CULTURE 2007 and Hercules. Israel has also expressed the interest in cooperating with several European agencies and/or bodies, for example the EEA, ENISA, EUROPOL, EUROJUST, CEPOL, ESA, etc.

The Action Plan is a process. It is in the early stages of implementation and it is too early to draw overall conclusions. During the remaining period of the Action Plan's life, the further development of EU-Israel relations will depend on the degree of commitment of both sides to the common values and principles agreed in the Action Plan. In addition to the political dialogue, an important issue is the question of convergence of Israeli and EU policies, especially in areas relating to the Single Market and other Community policies. Some in Israel wish to promote a European path towards greater economic and social convergence; for others, this is controversial. The degree to which EU-Israel relations can develop further will depend, *inter alia*, on the choices that Israel makes on this issue, and the response the EU is able to offer.

### **Political dialogue and co-operation**

In the Action Plan, both parties recognise the value of conducting a regular political dialogue on a wide spectrum of matters. Channels of communication have further expanded with the establishment of the political dialogue and cooperation subcommittees in 2005.

In the framework of the **sub-committee on political dialogue and co-operation** held in November 2005 special attention was devoted to the situation in the Middle East, the promotion and upholding of fundamental values such as human rights and democracy issues, minorities, all forms of racism and xenophobia, including anti-Semitism and Islamophobia.

On Middle East issues, the EU and Israel agreed in the Action Plan to strengthen political dialogue and identify areas for further co-operation, working together, on a bilateral basis and with the EU as a member of the Quartet, with the aim of reaching a comprehensive settlement of the Israeli/Palestinian conflict and a permanent two-state solution with Israel and a Palestinian state living side by side in peace and security, in accordance with the Roadmap, and the obligations of the parties set out in it.

In this context, in November 2005, Israel and the Palestinian Authority concluded an “**Agreement on Movement and Access**”, including agreed principles for Rafah crossing (Gaza) with the involvement of the EU as Third Party. This Agreement aimed at facilitating the movement of people and goods from and to Palestinian Territories.

The Council of the European Union (EU) then decided to launch the “**EU Border Assistance Mission for the Rafah crossing point**” (EU BAM Rafah), with the task to monitor the

operations of this border crossing point. This mission, which began on 26 November 2005 with an initial duration of one year, has been extended for a further 6 months.

In relation to this, the EU has recently recalled the utmost importance of the full implementation of the Agreement of Movement and Access, particularly the permanent opening of the Rafah, Karni and other crossings. It also reiterated its call for the immediate release of the abducted Israeli soldier and the immediate release of Palestinian Ministers and legislators in Israeli custody.

More generally, the European Council affirmed the view of the Quartet that the Hamas-led Palestinian Government needs to meet and implement the three principles of non-violence, recognition of Israel's right to exist and acceptance of existing agreements and obligations. It condemned violence against Palestinian civilians, as well as the launching of Qassam rockets against population centres in Israel. It called on the Palestinian Authority to take action to improve security and prevent terrorist attacks on Israel, including through the disarmament of groups engaged in violence and terror. It reiterated its condemnation of extra-judicial killings.

In relation to final status issues, the European Council called on Israel to desist from any action that threatens the viability of an agreed two-State solution, with particular concern expressed on settlement activities, the construction of the barrier on Palestinian land and activities in and around East Jerusalem as well as in the Jordan Valley. The EU confirmed that it will not recognise any change to the pre-1967 borders other than those agreed to by both sides.

Taking into consideration the desperate economic and humanitarian conditions in the Palestinian territories, the European Council and the Quartet decided in June 2006 that the EU should go ahead with the establishing of the **Temporary International Mechanism (TIM)**, aiming at taking care of immediate needs in the Palestinian territories. The EU has encouraged the Israeli Government to resume transfers of withheld Palestinian fiscal revenues, including via the TIM.

During the same subcommittee a certain number of seminars and meetings on matters of common concern were agreed upon:

- A bilateral seminar on **racism, xenophobia and anti-Semitism**, focusing inter alia on legal matters, education and anti-Semitic propaganda, including in the media, is currently under preparation and is scheduled for December 2006.
- A technical meeting on export control regimes in the context of the **non-proliferation of WMD** (Weapons of Mass Destruction).
- As regards **fight against terrorism**, three main themes were identified: (i) sharing best practices with a view to strengthening the co-operation on fight against terrorism financing (held in March 2006); (ii) prevention of radicalisation and terrorists' recruitment; and (iii) on the dilemmas and concerns faced by democracies in their fight against terrorism.

More recently (June 2006), two informal working groups on **Human Rights and International Organisations** met and engaged in a meaningful dialogue at experts level on a number of issues as detailed hereafter.

The **informal working group on human rights** provided an opportunity for discussing issues inter alia on the enhancement of the rights of **minorities, international humanitarian law**, relevant international conventions and protocols as well as the newly established **UN Human Rights Council**, thereby establishing a closer dialogue on these issues. In addition, participants also discussed the impact of the separation barrier and the restrictions of movement within the Palestinian territories, the difficulties faced by humanitarian NGOs to access to the Palestinian territories, the extra-judicial killings, and administrative detentions on the one side and on the other the impact of Palestinian Qassam rockets targeting Israel's inhabited areas causing civilian casualties.

The **informal working group on international organizations** addressed inter alia matters relating to Israel's participation in the United Nations and its agencies, the increased financial contribution of Israel to the UN agencies and programmes, the adoption of the UN resolution on "Holocaust remembrance" and the 29<sup>th</sup> International Conference of the Red Cross and Red Crescent Movement (June 2006) relating to the adoption of an additional distinctive emblem. During the same meeting, the Israeli delegation presented the international conference on "Deserts and Desertification – Challenges and Opportunities" which Israel will be hosting in November 2006.

### **Economic and social cooperation and development**

Continuing the recovery trend which began in 2004 and sustained by a robust domestic demand, Israel's gross domestic product (GDP) rose by an estimated 5.2% in 2005. Inflation has remained under control, even if inflationary pressures re-emerged during the second half of 2005. The consumer price index (CPI) rose month-on-month by 1.1 % in July 2005 and by 0.8 % in October 2005. Overall, Israel's CPI rose by 2.4% in 2005. The unemployment rate in May 2006 reached 8.9% of the active population.

During 2005, increasing competition and efficiency enhanced market confidence and fostered sustainable growth. The economic reform agenda for the near future embodies significant structural reforms. The economic recovery has created favourable conditions, conducive for the strengthening of the financial sector. Nonetheless, credit risks are still a challenge for regulatory authorities. Recent efforts to streamline the public sector and to strengthen competition in utilities as well as the recent privatisations in the banking system have encouraged increased investor confidence.

Confronted with relatively high levels of poverty amongst certain population categories, the authorities have taken a number of measures, which should lead to an increased minimum wage and targeted public investments. Cooperation in the field of social development has been limited. In line with the priorities set up in the Action Plan an in-depth dialogue between Israel and the EC on **social and employment issues** should be established, through convening the relevant sub-committee, which is one of the two that have not yet been convened.

As regards the banking sector, despite the growing economy, non-performing loans as a percentage of total loans averages about 10% for the banking system, mainly in the construction and real-estate sectors which are not yet involved in the recovery process.

Israel has made good progress in addressing **sustainable development** issues. A 2003 Government decision requires each ministry to develop its own implementation plan. Work is well advanced on these plans with a number of them completed and foreseen results beginning to be achieved. An inter-ministerial committee, open to stakeholder representation,

has been created and in its second annual report observes that the integration of social aspects of sustainability and the promotion of sustainable consumption patterns are the biggest challenges facing Israel on its path towards sustainable development.

Since 1978 the **European Investment Bank (EIB)**, the long-term financing institution of the EU, has committed more than € 300 million to finance capital projects in Israel contributing to the country's economic development. Following recent contacts between the EIB and the relevant Israeli authorities, both parties have agreed to resume EIB operations in the country notably in the fields of infrastructure, environment and SME activities. However, this will only be possible once Israel has ratified a framework agreement with the EIB.

### **Trade-related issues, market and regulatory reform**

In the **trade-related field**, particular emphasis has been placed on actions focusing on policy and regulatory matters aimed at increasing trade relations and sustainable socio-economic growth. The priorities identified in the framework of the relevant sub-committee concentrate on measures which are key to strengthening economic activity and attracting investment.

In 2005, **EU-Israel trade** was strengthened, with Israel and EU exports to each other's markets up by 10.5% and 4.9% respectively, and two-way trade flows increasing to € 23 billion.

In order to promote further trade and investment, both parties agreed to establish a **business community dialogue** between EU and Israeli business leaders. The selection process of respective representatives is nearly completed and steps have been undertaken for the holding of the first dialogue's session in the first semester of 2007 to be hosted by Israel.

As a further sign of the increasing importance of the EU-Israeli bilateral **trade** relations, an **Israel-EU Chamber of Commerce**, which complements existing bilateral chambers of EU Member-States, was established in July 2006.

In June 2006, the EU and Israel initiated **negotiations** for the further **liberalisation of trade in agricultural, processed agricultural and fishery products**.

Both parties have also agreed to work towards the adoption of an efficient and proportionate **"dispute settlement mechanism"** establishing a more effective and streamlined mechanism specifically applicable to trade.

Israel adopted the Pan Euro-Mediterranean Protocol on Cumulation of **Origin** which is in force since January 2006. The Jordan-Israel Trade and Co-operation Agreement has been amended and **diagonal cumulation** between Israel and Jordan is applicable since July 2006. Israel will also be able to cumulate with EFTA and with Turkey. Also, in the **customs** sector, both parties have agreed to increase the exchange of information and experience, through technical meetings.

In 2005, a trilateral working group on trade was established between the European Commission, Israel and the Palestinian Authority with the objective of increasing technical cooperation between Israel and the PA. Implementation of this initiative has been suspended in the light of the current situation in the region. The Commission stands ready to relaunch these talks as soon as the political circumstances allow.

On **free movement of goods and technical regulations**, Israel has confirmed its commitment to negotiate an Agreement of Conformity Assessment and Acceptance of Industrial Products (ACAA) and selected the priority sectors to be included. A draft law on pressure equipment is under preparation, as are a draft ordinance on good manufacturing practices and a law on medical devices.

As regards **consumer protection**, Israel has shown strong interest in exchanging experiences with EU Member States and within the EU's Rapid Alert System for Non Food products (RAPEX). Israel is still reviewing the requirements and potential benefits of possible participation.

Israel increased its dialogue with the Commission on **sanitary and phytosanitary** issues, notably in the context of the relevant subcommittees and through the 2005 Commission (Food and Veterinary) visit on control and certification of plant exports to the EU. Within the framework of these subcommittees, some trade irritants have been finally resolved allowing better market access for some agriculture products. Israel took measures to combat the 2006 avian influenza outbreak. As a result, EU import restrictions to poultry and poultry products from Israel were finally lifted during 2006.

Israel has continued to take measures to improve the **investment** climate, particularly by accelerating privatisation and encouraging the development and liberalisation of capital markets. In late 2005, the Israel Accounting Board decided to introduce the International Financial Reporting Standards for all public companies as of 2008. This will not, however, apply to banks which use other accounting standards. Following the publication of the recommendations of an expert' group, work is progressing on the adoption of a code of corporate governance.

As regards **services**, Israel has started negotiations for an Economic Integration Agreement on Liberalisation of Services and Establishment. Regarding financial services, the Banking Supervision Department has directed banks to prepare for the implementation of Basle core principles for effective banking supervision by 2009.

Israel and the Commission have agreed to increase the exchange of information and experience, in the context of the relevant subcommittee, in the area of **taxation**. Contacts have been established for an exchange of views on the principles of the code of conduct for business taxation in specific fields of relevance. Discussion on this issue needs to be pursued. Israel negotiated new treaties on avoidance of double-taxation with three EU Member States.

In the area of **Intellectual Property Rights**, Israel has regrettably, and against the spirit of the Action Plan, adopted new legislation that provides inadequate protection against unfair commercial use of test data submitted by pharmaceutical companies and has reduced and made patent term extension granted to pharmaceutical companies more difficult.

In the field of **public procurement**, in the context of the WTO Agreement on Government Procurement, Israel agreed to reduce the value of its offsets, and to expand the scope of opened sectors (in services).

A conference on **statistics** to be organised by the Israeli central bureau of statistics, originally scheduled for 2006, will be replaced by a smaller-scale seminar in 2007 focusing on EU and international statistical methods. There has been little progress in developing a national strategy for raising awareness in Israel of EU and international statistical methods.

On **enterprise policy**, Israel is well advanced in the implementation of the Euro-Mediterranean Charter for Enterprise, in particular as regards research and innovation, as well as the development of the venture capital market. The planned initiative to introduce a one-stop-shop system has not been implemented yet.

No real progress has yet been made as concerns increased transparency in the field of state aid.

### **Co-operation in Justice and Home Affairs**

During the first year of implementation of the cooperation in the field of **Justice and Home Affairs**, particular emphasis was placed on the international response required in the fight against terrorism. In cooperating with all partners, the EU stresses that the commitment to combating terrorism must be carried out in full respect for international law, including international humanitarian law, human rights, fundamental freedoms and the rule of law. Focus has been placed on the response to terrorism which must also address the factors contributing to radicalisation and recruitment and curbing terrorist access to financial and other economic resources.

Against this background, EU-Israel co-operation has substantially increased through a number of initiatives.

In the **fight against money laundering**, the Committee of ministers of the Council of Europe gave a favourable opinion in January 2006 about the **participation of Israel as “active observer”** in **MONEYVAL** (Council of Europe restricted committee promoting the application of the FATF (Financial Action Task Force) standards on the fight against money laundering).

In February 2005, the Justice and Home Affairs Council adopted the decision to give a mandate to **Europol** to negotiate an **agreement** with Israel. Europol aims at improving the effectiveness and co-operation between the competent authorities in preventing and combating terrorism, unlawful drug trafficking and other serious forms of international organised crime. EUROPOL is currently assessing Israel’s Data Protection legislation.

The 75th **INTERPOL** General Assembly held in Rio de Janeiro in September 2006 approved Israel’s application for membership in the **European Regional Conference**. This will enable European and Israeli specialists on investigation and prevention of any particular kind of crime to meet and discuss matters of common concern.

In March 2006, the EU hosted a **seminar** in Brussels on “sharing best practices on **fighting terrorism financing**”, an issue of common concern, with the participation *inter alia* of the EU counter-terrorism Co-ordinator and high-ranking officials from the EU institutions and bodies and the Israeli Government. The technical discussion covered a number of issues ranging from the Israeli experience in fighting terrorism-financing to different EU initiatives undertaken in this field, from the implementation of the FATF special recommendation on terrorism financing to Israel’s and EU’s relevant co-operation with third countries.

Israel also initiated contacts with the aim to develop co-operation with **EUROJUST**, whose main tasks are to improve coordination and co-operation between investigators and prosecutors dealing with serious international crime. **EUROJUST** already has **contact points** in several third countries including Israel.

The European Commission and Israel have furthermore agreed to strengthen their co-operation in fighting against cyber-crimes, by definition borderless, *inter alia* through the development of Israel's co-operation with **ENISA** (European Network and Information Security Agency) which could help to prevent and respond to major network and information security problems.

A seminar on **human trafficking**, organised with the financial support of the European Commission, is scheduled to be held in Israel in December 2006, involving Israeli Government officials and representatives of civil society aiming at exchanging experience with EU Member States administrations about tackling this ever-growing phenomenon.

## **Transport, energy, information society, environment and science and technology**

### ***Transport***

Israel is implementing a **transport** policy of sustainable sector development against the background of a strong increase in traffic. Israel is executing a comprehensive **investment** programme of upgrading and developing infrastructure, in particular in the railway sector with a view to achieving a modal shift towards the increased use of public transport. In the road sector, the focus is on increasing **road safety** and extending the application of intelligent transport systems. In this respect, with the aim of exchanging experience and best practices developed in EU Member States, a series of thematic seminars is planned for the forthcoming months.

In 2005 the Israeli Ministry of transport was substantially reformed, with core departments upgraded and both the former civil aviation administration as well as the former shipping & ports administration were transformed into statutory authorities within the Ministry of transport. Israel has implemented a **port reform** in order to generate competition and increase efficiency in the sector. The Israel ports authority has been replaced with four companies, i.e. three port-operating companies and the Israel Ports Development & Assets Company. Regulatory oversight over these four companies is the responsibility of the newly created shipping and ports authority under the jurisdiction of the Ministry of transport.

Israel has not yet negotiated a horizontal aviation agreement with the Community, amending its bilateral air services agreements with EU Member States. In the field of aviation, a two-day workshop on **SESAR** (the Air Traffic Management Modernisation Programme for Europe) was held in June 2006 in Jerusalem. Preliminary discussions with Israel on a possible participation to the SESAR project have started.

Since 2004, Israel participates in the **Galileo** Programme, a joint initiative of the European Commission and the European Space Agency (ESA) to provide Europe with its own independent global civilian controlled satellite navigation system. In September 2005 MATIMOP became a member of the Galileo Joint Undertaking. MATIMOP is a non-profit organisation under the Israeli Ministry of Industry, Trade and Labour, promoting technological and R&D cooperation and technology transfer activities between Israeli and foreign industries.

At sub-regional level, transport constitutes a topic of strategic importance in Israeli – Palestinian cooperation. The two parties agreed in 2005 to set up a **Joint Transport Office (JTO)** to promote transport cooperation. Implementation of this initiative has been suspended in the light of the current situation in the region.

## *Energy*

In the framework of the relevant sub-committee, both parties acknowledged Israel's and the EU's mutual interest in enhancing co-operation and dialogue on **energy**, notably on internal electricity and gas markets, the promotion of energy efficiency and the use of renewable energy.

The Israeli draft Energy Master Plan is being updated and is expected to be completed in 2007. Israel is considering the possibilities to opening up its gas and electricity markets. Israel has also continued to enhance gas use in the economy (notably for power generation) and pursued the expansion of the domestic gas network. A gas supply contract with Egypt was signed in 2005 and the associated import pipeline is being constructed. Israel is considering complementary gas supply options including from offshore fields, Russia and the Caspian region.

With the financial support of the European Commission, a financing agreement was signed in December 2005 to implement a three-year **Israeli-Palestinian Energy Cooperation Programme** including the establishment of a joint energy office. Implementation of this initiative has been suspended in the light of the current situation in the region.

## *Information society*

As regards the **information society** sector, Israel has not yet established a regulatory authority for electronic communications. The market for wireless handsets has been opened to competition in 2005. In 2006, the mobile operator Cellcom was granted a fixed telephony licence to compete with the incumbent network operator Bezeq.

Regarding **audiovisual policy**, a new regulatory concept is being developed.

## *Environment*

In the **environment** field, the European Commission and Israel have enhanced co-operation and information exchange on a wide range of issues, including on environmental taxes, eco-management, spatial planning, air pollution, water and waste issues, coastal erosion, climate change, capacity building at communities' level, environmental procurement practices within local authorities, sustainable impact assessment, and sustainable development aspects of the Jordan River. A number of other topics, including with respect to the European Environment Agency, have been identified for closer co-operation.

Key environment issues relate to air quality, water resources and water quality, waste management, nature protection and industrial pollution. Israel has continued to make progress on climate change as national structures have been set-up, procedures for the clean development mechanism (CDM) adopted, and several CDM projects prepared. Framework and sectoral legislations are in place in most areas. Latest environment legislation includes laws on used tyre recycling, coastal erosion, non-ionising radiation and prevention of water pollution from fuel pipelines. Israel publishes environmental information on a regular basis and a 2005 amendment to the freedom of information law aims to make environmental information held by Government agencies more accessible. Israel publishes environmental information on a regular basis. The Ministry of Environment has taken steps to promote the involvement of NGOs, also as regards regional co-operation. While administrative structures on environment are in place, these still need to be strengthened. There are several ongoing

activities to integrate environment considerations into other policy sectors. Israel has ratified relevant international and regional conventions and protocols, including the amended Convention for the Protection of the Marine Environment and the Coastal Region of the Mediterranean (Barcelona Convention). Israel is currently working to ratify the Land-Based Sources Protocol and the Special Protected Areas Protocol of the Barcelona Convention). Israel participates in the Mediterranean Action Plan (MAP) as well as the Euro-Med Water Directors Conference.

### *Science and technology, research and development*

Israel has been fully associated to Community R&D Framework Programmes (FP) since 1996 and by the middle of 2006 more than 500 Israeli entities participated in projects funded under FP 6 with a particularly strong participation in the areas of information technology and life sciences. In October 2006, the Commission requested a mandate from Council to negotiate an agreement with Israel on its association to the 7<sup>th</sup> Research Framework Programme (2007-2013).

### **People-to-people contacts**

Policy dialogue with Israel on education has focused on clarifying interests and options for extending existing cooperation in **education and training**. In this respect, the Commission services and relevant Israeli authorities met in Brussels in May 2006 with the aim of exploring the scope of a strengthened bilateral and multilateral cooperation in the area of higher education. Moreover, the **Euro-Med Youth** programme supports projects for Israeli youth.