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EU DIFFERENTIATION AND ISRAELI SETTLEMENTS

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SUMMARY

- The EU has implemented a de facto policy of differentiating between Israel and settlement activities in the Occupied Territories within its bilateral relations. The EU's legal requirement to comply with its own non-recognition of Israeli settlement activity has resulted in a nascent, legally driven, consensus around differentiation.
- Differentiation is one of most impactful tools at the EU's disposal for challenging the incentive structure underpinning Israeli support for the status quo. The EU and its member states must acknowledge and own differentiation as a fully-fledged policy by giving it a name and referencing it in official statements issued at the senior political level.
- European leaders should actively defend differentiation from increasingly forceful efforts by Israel's political class to misrepresent and conflate EU actions with a boycott of Israel. Differentiation does not stem from a desire to isolate Israel, but rather from deepening EU-Israel ties and EU legal obligations.
- Stepping up differentiation is consistent with past EU statements and conducive to the EU's policy objectives. This report outlines several areas where the logic of differentiation calls for further consideration and legal analysis in order to achieve broader, coherent and consistent implementation.

Europe has maintained a longstanding commitment to two cardinal tenets: its strong historic close ties with Israel and a resolution of the Israel/Palestine conflict based on two states. A Palestinian state living peacefully alongside Israel is one of the most enduring European Union Common Foreign Security Policy positions, the origins of which can be found in the 1980 Venice Declaration issued by the then nine-member European Economic Community (EEC). This is one of the areas most invested in by common European policy in terms of funding, political energy, and time dedicated.

Over the years, European and Israeli leaders have worked assiduously to avoid tension in having to choose between those twin goals of thickening EU-Israel ties and pursuing peace. The effort to insulate both tracks has been largely successful but is now becoming increasingly untenable in one area – an issue around which a nascent European consensus exists – the need to differentiate between Israel and its settlements project in the day-to-day conduct of bilateral relations. The EU and its member states, like the rest of the international community, do not recognise any legal or de facto Israeli sovereignty over the Occupied Palestinian Territories (OPTs). This duty of non-recognition is based on international law, resulting in a legal obligation to clearly differentiate between Israel and its activities beyond the Green Line within their bilateral relations.

Paradoxically, this point of both potential tension and leverage is born not of any European animus towards or shunning of Israel, but precisely as a consequence of the depth, breadth, and closeness of European-Israeli ties. Inclusion of Israeli activity beyond the pre-1967 lines (the Green Line, considered by longstanding EU policies as delimiting Israel's territorial sovereign area of jurisdiction

and as the basis for a future two-state peace deal) therefore cannot be part of those thickening bilateral EU–Israel ties. That same Israeli matrix of control inside the OPTs also happens to be antithetical to a two-state outcome.

This tension between thickening EU–Israel ties and Europe’s long-held political and legal position about the Israeli–Palestinian conflict has, particularly in the past decade, produced an EU de facto policy of differentiation between Israel and its activities beyond the Green Line. The political mandate for the EU’s differentiation practices came from a number of Foreign Affairs Council (FAC) conclusions issued from 2009 onwards; the most recent in July 2015. So far, the most visible examples of the application of this nascent policy have been the issuing of the European Commission’s July 2013 guidelines on EU funding and the requirements placed on Israel’s membership to Horizon 2020, the EU’s flagship research and development (R&D) programme. However, having been established in practice, the policy of differentiation has not been sufficiently acknowledged or implemented in a consistent way, apparently out of concern that such measures might interfere with on-again, off-again peace negotiations.

That source of hesitation has become harder to defend given the repeated failures of the Middle East Peace Process (MEPP), as it is currently configured, in offering any path towards a viable settlement or even being resilient enough to continue to provide an effective tool for conflict management. One consequence of Oslo’s failure is that in Israel there is now something of a consensus that the settlement enterprise can be managed and expanded without incurring any tangible costs. Consequently, Israel’s political leaders and voting public can discount the OPTs and settlement issue to an unprecedented degree as they go about their daily lives, make their political choices, and set their governing policies.

As Israel’s largest trading partner, Europe leads in either confirming or bucking this perception. There is therefore, alongside the legal obligation, a strong political rationale for differentiation. Besides stemming from Europe’s compliance with its own positions and regulations in its dealings with Israel, differentiation can help in changing the structure of incentives that underpin Israel’s settlement policy. Europe’s almost ritualistic condemnation of Israeli settlements and violations of international law in the OPTs has been largely dismissed as background noise or a minor nuisance by Israeli governments over the years and has not held back the deepening of EU–Israel ties. This approach has, by any measure, been spectacularly ineffective in impacting on Israeli policy.

The potentially impactful nature of a more consistently applied EU differentiation policy probably explains why Israel’s leaders have assumed such an assertive posture in opposing it. Many Israeli political leaders, including Prime Minister Benjamin Netanyahu, have wrongly and perhaps intentionally misrepresented EU differentiation as part of efforts to boycott Israel and have conflated it with the grassroots “Boycott, Divestment and Sanctions” (BDS) campaign. But the genesis, goals, and policies that flow from differentiation contrast starkly with those of BDS. One

is premised on the deeper integration of Israel with Europe, the other on its isolation. Some Israeli politicians have even gone as far as equating EU differentiation as a manifestation of European anti-Semitism that seeks to de-legitimise Israel.

To push back against this smear campaign first and foremost requires Europeans to articulate what exactly they are doing with differentiation and why, and to do so in a consistent, coherent, and collective manner – and at the highest levels. By allowing Israel to negatively define the policy by default, Europe misses the chance to make clear that this is not a discriminatory measure but the legal consequence of Israel’s attempts to integrate economically with Europe while making the illegal settlements part of that integration.

Quite simply, Europeans now have to own and defend the policy that they have already been de facto pursuing but which they have been reluctant to explicitly acknowledge in the highest-level political engagements with their Israeli interlocutors. The central theme of the pushback should be the legal imperative to draw this differentiation unless or until Israel either makes the same differentiation itself or ends its settlement and occupation policy (or indeed produces an alternative and agreed solution for the OPTs that is recognised internationally).

This policy also needs to be explicitly named (including clear reference in FAC conclusions), messaged around, better explained, and defended against attacks by Israel’s political class. Owning, naming, and deepening this policy is more likely to contribute to a viable settlement than to impede it by changing the cost/benefit calculations of Israelis towards the status quo. Indeed, the history of differentiation thus far indicates that when it has been applied, it has led to a debate within Israel in which the contradictions between maintaining the settlements and thickening (or simply continuing) current relations with Europe have emerged. Having been named and explained, differentiation should then be deepened and expanded in order to bring the EU’s day-to-day policies consistently in line with its own legislation and principles. Given the extent to which Israeli settlements have been integrated into the workings of everyday Israel, the furtherance of the EU differentiation policy could actually pose real dilemmas for Israel while helping to preserve the possibility of a two-state outcome.

This paper looks in detail at what has until now been a de facto differentiation policy and explores the steps that could be taken to put it into effect more consistently. It does not address European–Palestinian bilateral relations or indeed Palestinian strategies towards the conflict. Clearly, the Palestinian leadership too has agency and responsibilities in relation to resolving the conflict, but the Palestinians are not the driving force behind differentiation; Europe’s own position as a normative actor and European–Israeli dynamics are the key factors in this story. Differentiation is of course just one track to be pursued by the EU and cannot be a substitute for a broader strategic rethink towards the conflict. But if Europe wants to at least preserve the possibility of a two-state outcome and help create the conditions in which meaningful negotiations can ultimately be re-launched, then differentiation can act as a potentially significant tool

with which to challenge the cost/benefit calculations of the Israeli public as well as of political and other elites regarding continued occupation. Moreover, it is currently the most politically feasible and potentially impactful policy at the EU's disposal. It is also in line with the EU's longstanding positions on Israel's occupation of Palestinian territory and its obligations under international law.

Thickening EU–Israel ties

For decades, the EU, and especially its member states, have largely insulated the practical functioning of their bilateral relations with Israel from the Palestinian issue, the occupation, and European attempts at peacemaking. Israel is part of the Euro-Mediterranean Partnership (Euromed) that promotes economic integration and democratic reform across the EU's southern neighbourhood (i.e. North Africa and the Middle East). Within this framework, an Association Agreement was signed in November 1995 that deepened EU–Israel relations and enabled close cooperation across a range of areas relating to trade, tourism, hi-tech, the military, and education. Also thanks to this development, the EU has continued to be Israel's foremost trading partner, with total trade amounting to approximately €29 billion in 2013.¹

In 2009, the EU decided to suspend all upgrades in its relations with Israel and put on hold negotiations on a new Association Agreement pending a peace agreement with the Palestinians. This, however, has not stopped the European Commission from exploiting existing opportunities to continue thickening economic and cultural relations under the existing 2005 European Neighbourhood Policy (ENP) Action Plan, which, as it happens, are manifold.² In January 2010, the EU was therefore able to implement an agreement reached with Israel in 2008 allowing for the opening up of additional agricultural trade. Additionally, a meeting of the EU–Israel Association Council in July 2012 identified a list of 60 concrete actions in 15 fields whereby the EU–Israel relationship could be further tightened.³ In other words, Israel has hardly felt the current freeze.

Israel received €13.5 million between 2007 and 2013 as part of the European Neighbourhood and Partnership Instrument (ENPI), the main EU financial instrument for funding development cooperation programmes with the neighbourhood partner countries. Although a relatively modest figure, this has allowed Israel to benefit from the EU's Erasmus Mundus programme, which enhances mobility and cooperation with the EU in the field of higher education, as well as the Tempus programme, which supports the modernisation of higher education. Since 2007, Israel has been part of the EU's "Twinning" instrument, which promotes joint projects in the areas of data protection, urban transport, equal employment opportunities, veterinary inspection, and telecommunications.⁴

1 EU–Israel trade data is available on the European Commission's website at <http://ec.europa.eu/trade/policy/countries-and-regions/countries/israel/>.

2 Krassimir Y. Nikolov, "Ashton's Second hat: The EU Funding Guidelines on Israel as a Post-Lisbon Instrument of European Foreign Policy Making", *Diplomacy*, 6 October 2014, available at <http://diplomacy.bg/archives/1299?lang=en> (hereafter, Nikolov, "Ashton's Second hat").

3 For more details, see the Council of the European Union's statement on the Eleventh Meeting of the EU–Israel Association Council, 24 July 2012, available at http://www.europarl.europa.eu/meetdocs/2009_2014/documents/d-il/dv/eu-israelassociationcouncilstatement/eu-israelassociationcouncilstatementen.pdf.

4 A full overview of EU international cooperation and development agreements with Israel can be found on the European Commission's website at <https://ec.europa.eu/europeaid/node/461>.

Along with all this, Israel is expected to receive €900 million in inbound research grants and other investments in return as part of Horizon 2020. Based on an initial investment of €600 million, this will make Israel a significant net beneficiary of the programme.⁵ Access to EU R&D funds through the EU's previous framework programme for research and technological development – FP7 – between 2007 and 2013 enabled Israel to receive a further €782 million, through which it participated in 1,536 projects.⁶ Moreover, Israel is the only southern neighbourhood country to be fully "associated" with Horizon 2020, allowing Israeli entities to participate under the same conditions as member states.⁷ This also permits Israel to participate in Programme Committee meetings determining Horizon 2020's strategic direction.

Erasing the Green Line

Unlike East Jerusalem, Israel has not officially annexed the West Bank. Yet successive Israeli governments have made considerable efforts to integrate the settlements as fully as possible into the country's day-to-day workings. A network of Israeli-only roads running through the West Bank connects Israeli settlements with Israel and to each other while bypassing Palestinian population centres. Settlements, meanwhile, are fully integrated into Israel's national power grid and water carrier system, while settlers communicate using the services and infrastructure, including large installations such as antennae, of all four of Israel's main telecommunications companies.

Settlements also play a role in Israeli society like any other town or city inside the Green Line. The settlement of Ariel, for example, houses one of Israel's eight universities. And five settlement football teams (Ma'aleh Adumim, Ariel, Kiryat Arba, Bik'at Hayarden, and Givat Ze'ev) currently play in Israel's national football league, which is a member of the Union of the European Football Associations (UEFA).

At first glance, settlements only contribute about 4 percent of Israel's total GDP and less than 1 percent of total Israeli exports to the EU (around €230 million).⁸ Yet they are a crucial component of the current system of occupation and control of the West Bank, something that has stymied Palestinian statehood and limited the viability of the Palestinian Authority (PA). The 1995 Oslo II Accords and subsequent agreements in the late 1990s divided the West Bank territory into three areas: Area A (17.2 percent), under the control of the PA; Area B (23.8 percent), under Palestinian civil administration and joint Israeli-Palestinian security control; and Area C (59 percent), under full Israeli

5 Soeren Kern, "EU, Israel Reach 'Compromise' on Science vs. Settlements", *Gatestone Institute*, 27 November 2013, available at <http://www.gatestoneinstitute.org/4068/eu-israel-horizon>.

6 "Israel 'vital candidates' for Horizon 2020", *Horizon 2020 Projects*, 5 March 2014, available at <http://horizon2020projects.com/global-collaboration/israel-vital-candidates-for-horizon-2020/>.

7 For more details on countries associated with Horizon 2020, see the European Commission's factsheet, available at http://ec.europa.eu/research/participants/data/ref/h2020/grants_manual/hi/3cpart/h2020-hi-list-ac_en.pdf.

8 For more information, see the report by 22 NGOs, "Trading Away Peace: How Europe helps sustain illegal Israeli settlements", 30 October 2012, available at <https://www.fidh.org/International-Federation-for-Human-Rights/north-africa-middle-east/israel-occupied-palestinian-territories/Trading-Away-Peace-How-Europe-12343>.

control.⁹ The control that Israel exercises over Area C gives its economy exclusive access to important natural resources located in the West Bank, including water aquifers and quarries. Palestinian businesses and farms are barred from accessing these resources, permitting them to develop in Area C could add as much as 35 percent to their GDP.¹⁰ Moreover, according to the overwhelming body of international legal opinion, as an occupying power Israel is prohibited from deriving any economic or financial benefit from the occupied territories.¹¹

Support for the settlements cuts across the political spectrum. Since Israel's capture of the Palestinian Territories in 1967, every Israeli government has promoted construction there. Under Prime Minister Benjamin Netanyahu since 2009, spending on settlements has reportedly risen by a third¹², with the central government reported to have contributed €825 per capita per year to support settlements, two-thirds higher than the national average.¹³ At the same time, settlements enjoy preferential economic investments – from expanded budgeting to tax benefits through “one-off” grants and subsidised loans – thanks to their designation as National Priority Regions. The ministries of agriculture and tourism have also played their part in encouraging businesses to move to or expand opportunities in the West Bank. The former contributed some €5 million to agricultural projects within the West Bank between 2008 and 2010, with the figure set to have risen since then.¹⁴ None of this would be possible were it not for Israeli banks such as Bank Hapoalim, Bank Leumi, and Bank Mizrahi Tefahot, all of which provide mortgages for settler homes and loans to West Bank regional councils and finance infrastructure construction for the settlements themselves, such as the Jerusalem Light Rail project.

The EU's nascent differentiation policy

The EU has never recognised the legality of Israeli settlements in the occupied territories (including those in East Jerusalem and the Syrian Golan Heights that have been formally annexed by Israel) and consequently does not consider agreements signed with Israel to also apply to Israeli settlement-based entities. This distinction has, however, not always been enforced in practice. Not only because Israel has sought to erase the Green Line on the ground, but also due to the fact that as cooperation with Israel

9 Within the Israeli-controlled Area C, Israel applies a mixture of Ottoman, British Mandate, Jordanian, and Egyptian laws, as well as Israeli military orders, to Palestinians. But Israeli settlers throughout the Occupied Palestinian Territories (OPTs) in addition to any Israeli present in the OPTs, are subject to Israeli law.

10 See “Palestinian Access to Area C Key to Economic Recovery and Sustainable Growth”, the World Bank, Jerusalem, 8 October 2013, available at <http://www.worldbank.org/en/news/press-release/2013/10/07/palestinians-access-area-c-economic-recovery-sustainable-growth>.

11 See article 53 and 55 of the Fourth Geneva Convention relative to the Protection of Civilian Persons in Time of War (1949); as well as articles 46 and 55 of the Fourth Convention of the Hague Regulations concerning the Laws and Customs of War on Land (1907).

12 Maayan Lubell, “As costs rise, Israeli settlements face questions at home”, Reuters, 24 June 2014, available at www.reuters.com/article/2014/06/24/us-palestinian-israel-settlements-idUSKBN0EZOJA20140624 (hereafter, Lubell, “As costs rise, Israeli settlements face questions at home”).

13 Lubell, “As costs rise, Israeli settlements face questions at home”.

14 “Forbidden Fruit: The Israeli Wine Industry and the Occupation”, Who Profits, April 2011, available at <http://www.whoprofits.org/sites/default/files/WhoProfits-IsraeliWines.pdf> (hereafter, “Forbidden Fruit: The Israeli Wine Industry and the Occupation”, Who Profits).

expanded in the 1990s, the EU treated Israel's occupation as temporary in the belief that the imminent success of the Oslo peace process would make added clarifications a moot point. The EU therefore avoided implementing a legal regime of differentiation during this period, and, as a result, its 1995 Association Agreement with Israel did not contain an explicit territorial clause.

The optimism of the early 1990s seems a long time ago, and a number of subsequent developments have fed a “general malaise” in EU policy towards the conflict, as European External Action Service (EEAS) official Krassimir Nikolov has described it:¹⁵

- i. the collapse of the Oslo peace process and the acknowledgement that Israel's occupation would be an enduring feature of EU–Israel relations;
- ii. acknowledgement that the peace process in its current configuration cannot result in a viable peace agreement, with settlement expansion and Israeli political rhetoric central to that impasse;
- iii. the mutually exclusive territorial scopes that resulted from the 1997 Interim Association Agreement on trade and cooperation with the Palestine Liberation Organization and the 1995 Association Agreement with Israel, and questions as to which (if either) of these two agreements covered Israeli settlements; and
- iv. Israeli settlement policies becoming ever more egregious, with increasingly ritualistic European condemnations and opposition being dismissed by Israel.

On the level of EU actions, increasing pressure from NGOs and the European Parliament, as well as mounting frustration within the European Commission and in many member states over the lack of progress towards the two-state solution have forced the EU to pay greater attention in delineating the territorial scope of agreements entered into with Israel as well as the territorial limitations to international agreements signed by Israel. The European Court of Justice (ECJ) added a further legal push in this direction in February 2010 when it ruled that agreements reached with Israel must be interpreted in light of the EU's agreement with the PLO, and therefore only the Palestinian authorities can issue origin certificates for goods originating in the West Bank, including from Israeli settlements.¹⁶ As a result, the European Commission and the EEAS have gradually been compelled to take greater care in ensuring the EU's correct adherence to European law in its bilateral relations with Israel. The constellation of ad-hoc initiatives that ensued – of which the below actions are the main examples – steadily crystallised into an unarticulated policy of “differentiation”, albeit one that is so far not sufficiently explained, defended, or consistently applied.

On the declarative and legal levels, the EU has always maintained that the law of occupation applies to the Palestinian Territories and that Israeli settlements are

15 Nikolov, “Ashton's Second hat”.

16 Itzhak Kornfeld, “ECJ Holds that West Bank Products are Outside Scope of the EU–Israel Association Agreement”, American Society of International Law, Insights, Volume 14, Issue 17, 23 June 2010, available at <http://www.asil.org/insights/volume/14/issue/17/ecj-holds-west-bank-products-are-outside-scope-eu-israel-association>.

consequently illegal. As an occupying power, Israel is also prohibited from deriving any economic or financial benefit from the Occupied Palestinian Territories. These positions are predicated on international law and an overwhelming body of international legal opinions, including from the International Court of Justice (ICJ) and the ECJ, and are also shared by the United States and every other country in the world with the exception of Israel. Numerous statements by the FAC have continuously re-emphasised the EU's non-recognition of Israeli settlements. This culminated in a commitment in May 2012 "to fully and effectively implement existing EU legislation and the bilateral arrangements applicable to settlement products"¹⁷, and, in December 2012, towards ensuring that all its agreements with Israel "unequivocally and explicitly indicate their inapplicability to the territories occupied by Israel in 1967".¹⁸ The FAC conclusions issued in July 2015 re-affirmed these two commitments.¹⁹

The differentiation policy has since affected EU dealings with Israel on several issues.

Rules of origin

The EU (or ECC as it was previously known) has maintained free trade agreements (FTAs) with Israel since 1977. Most recently the EU's Association Agreement with Israel has allowed products from both sides to benefit from preferential trade tariffs. In February 2005, the parties reached a technical arrangement in order to tighten the exclusion of Israeli goods produced in Israeli settlements located within the "territories brought under Israeli administration since June 1967" (i.e. East Jerusalem, the West Bank, and the Golan Heights).²⁰ In order to implement this measure, the EU drew up a list of Israeli "settlement" postcodes in cooperation with Israel. Goods bearing one of those postcodes are consequently denied preferential access to EU markets.

EU FTA regulations do not exclude Israeli products containing materials obtained from the occupied territories from receiving preferential tariffs "provided that the said materials have undergone sufficient working or processing in Israel".²¹ So for example, Israeli wine exporters using a non-settlement postcode continue to claim preferential tariff treatment despite using grapes from West Bank settlements. Likewise, it seems that products from Israeli cosmetics company Ahava are also entitled to the same preferential treatment given their use of a non-settlement postcode and the location of one of their factories west of the Green Line in Ein Gedi.²² This, even though Ahava products contain

¹⁷ Council conclusions on the Middle East Peace Process, 14 May 2012, available at https://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/EN/foraff/130195.pdf.

¹⁸ Council conclusions on the Middle East Peace Process, 10 December 2012, available at http://ceas.europa.eu/delegations/israel/press_corner/all_news/news/2012/20121210_02_en.htm.

¹⁹ Council conclusions on the Middle East Peace Process, 20 July 2015, available at <http://www.consilium.europa.eu/en/press/press-releases/2015/07/20-fac-mepp-conclusions>.

²⁰ Details on the EU-Israel Technical Arrangement (including non-eligible Israeli postcodes) are available at http://ec.europa.eu/taxation_customs/customs/customs_duties/rules_origin/preferential/israel_ta_en.htm.

²¹ See Protocol 4 of the EU-Israel Association Agreement, which defines the concept of originating products, available at http://ceas.europa.eu/delegations/israel/documents/eu_israel ASSO agree_en.pdf.

²² ECFR interview with European Commission officials, April 2015.

Dead Sea minerals from the OPTs.²³

Monitoring and enforcing Israeli compliance with EU FTA rules largely falls to the customs agencies within individual member states. Their focus has been on investigating the falsification of proofs of origin (including EUR.1 movement certificates) or instances when insufficient information has been supplied to establish the origin of a product. For example, in the United Kingdom alone, customs authorities discovered 529 cases between January and April 2009 in which settlement products were falsely declared to have originated from within Israel.²⁴

Little attention, though, is paid to the actual chain of production in order to ensure that material from the OPTs used in products "originating" in Israel has indeed been sufficiently transformed according to FTA criteria. These do not include repackaging, mixing products, animal slaughter, washing, shelling, and the like. In the case of food-related products, detailed information on this is readily available to European retailers (although not to customs officials) thanks to strict EU rules on the traceability of food products for health and safety reasons.

While many supermarkets do not currently distinguish between products from Israel or the settlements on their shelves (an issue unrelated to rules of origin), the European Commission has placed on them part of the responsibility for verifying the correct adherence of Israeli products to FTA regulations.²⁵ But unless a third-party complaint is made, there is little that compels national authorities to directly intervene at this level. Nor is the Israeli government compelled to verify or otherwise enforce adherence by Israeli exporters to EU FTA rules, although it has set up a dedicated budget that allows it to compensate settlement-based entities that suffer financial consequences as a result of EU regulations.

Delimiting territorial scope

The principle of "no recognition, no existence" towards settlements implies a limitation of EU recognition of the territorial extent of Israel's sovereign jurisdiction to within the Green Line. These have applied, for example, to the "open skies" civil aviation agreement reached between the two parties and, in theory, to the domains of personal data protection.

When correctly enforced, this principle also means that there is no legal way for the EU to recognise Israeli certification of settlement products – the consequence being that some animal-based and organic Israeli products from the OPTs are now ineligible for the EU market. Since the EU does not recognise Israel's sovereignty over the West Bank, it cannot recognise the on-site inspections carried out by the

²³ For more information on the use of West Bank materials in Israeli products, see the following Who Profits reports: "Forbidden Fruit: The Israeli Wine Industry and the Occupation" (see footnote 13) and "Ahava: Tracking the Trade Trail of Settlement Products", May 2012, available at <http://whoprofits.org/content/ahava-tracking-trade-trail-settlement-products>.

²⁴ See "Israeli settlement goods", the Ecumenical Council for Corporate Responsibility, available at <http://www.eccr.org.uk/module-htmlpages-display-pid-64.html> (hereafter, "Israeli settlement goods", ECCR).

²⁵ "Notice to importers – Imports from Israel into the EU", Official Journal of the European Union, 3 August 2012, available at http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.C_.2012.232.01.0005.01.ENG

Israeli certifying agency. The EU has therefore been unable to recognise Israeli certification of the organic status of settlement produce, nor can it recognise the certification of health standards for food products, such as verifying that poultry, eggs, and dairy are not contaminated with salmonella or other bacteria. As a result, the correct application by the EU of its own regulations has meant that these settlement products could no longer be cleared for EU markets.

Enforcement remains unclear though. Although Israel's Ministry of Agriculture has issued a general warning asking dairies to separate raw milk produced in the settlements from that produced within the Green Line, investigations carried out by the Who Profits research centre raise questions over the extent to which Israeli companies have acted to differentiate their production lines and the extent to which the EU is able to monitor or otherwise enforce compliance under current arrangements. One corrective opportunity in this respect could come from the yearly inspections by the EU Food and Veterinary Office, which verifies the traceability of products.

The EU's funding guidelines and Horizon 2020

Under European parliamentary pressure to ensure that no EU tax money finds its way into Israeli settlements, the European Commission published its July 2013 funding guidelines in which it explicitly states that Israeli settlement-based entities and activities are excluded from receiving EU financial grants, such as those available through Horizon 2020, as well as other EU programmes, such as Erasmus and Tempus.²⁶ While these guidelines are non-binding on EU member states, they have nonetheless acted as a useful template for those seeking to guarantee their own compliance with international law as applied to Israel and its settlements. This was the case for Germany, which, in January 2014, followed the EU's example by conditioning the disbursement of its own hi-tech and science grants for Israel on the exclusion of settlement entities.

In the case of Israeli participation in Horizon 2020, EU funding has been withheld for Israeli projects undertaken in the OPTs, even when conducted by Israeli entities based in Israel proper. For example, Tel Aviv University cannot use Horizon 2020 funding to conduct archaeological digs in the OPTs. Likewise, even though it maintains a registered address within Israel, the cosmetics company Ahava cannot use EU funding in the plant it operates in the West Bank settlement of Mitzpe Shalem. In comparison to FP7, which merely took into account the place of establishment of Israeli entities, the new Horizon 2020 criteria represented a tightening of EU rules on where and how EU funds could be spent. After long negotiations, Israel signed up to Horizon 2020 but included its own appendix to the agreement stating that it objected to the EU's guidelines excluding Israeli settlement-based entities for both legal and political reasons.²⁷

As the EEAS's Nikolov pointed out, though, these conditions

²⁶ Guidelines on the eligibility of Israeli entities and their activities in the territories occupied by Israel since June 1967 for grants, prizes and financial instruments funded by the EU from 2014 onwards", Official Journal of the European Union, 19 July 2013, available at http://eeas.europa.eu/delegations/israel/documents/related-links/20130719_guidelines_on_eligibility_of_israeli_entities_en.pdf.

²⁷ Barak Ravid, "Israel and EU compromise on terms of joint initiative, following rift over settlement funding ban", Haaretz, 26 November 2013, available at <http://www.haaretz.com/news/diplomacy-defense/.premium-1.560292>.

are still considerably softer than similar agreements reached between the US and Israel in 1972 and 1976, which looked at both the location of Israeli activities and their purpose. Actions that in any way pertain to Israeli settlements, according to these agreements, would be ineligible for funding, even when conducted outside the OPTs.²⁸

Within the framework of Horizon 2020, Israel and the EU also agreed on a joint EU–Israel monitoring mechanism to ensure that funds destined for Israeli entities within the Green Line would not be used as part of any activities conducted in the OPTs. The burden of proof largely rests on Israeli applicants by requiring each of them to sign a declaration on honour that they meet the EU funding criteria. The ultimate aim of this declaration was not to force Israeli entities to sign up to the EU's position on Israel's borders but to provide a legal basis to claim back its funding in case of an untruthful declaration. This also allows the EU to protect itself against the risk of illegality and legal claims against it.

The case of Horizon 2020 demonstrates where the potential for EU policy lies. With the notable exception of Ariel University, most of Israeli academia is situated within Israel's sovereign borders. Likewise, the vast majority of the Israeli R&D sector has little to do directly with the settlements. Even so, the largely pro-settlement Netanyahu cabinet rallied against the EU's funding guidelines and threatened to withdraw from Horizon 2020, promising "tough negotiations" with the EU to avoid submitting to "European dictates". Israel's politicians, though, were quickly restrained by the leadership of Israel's academic and research community, which insisted that the programme's funds and especially the cooperation with Europeans it fostered were essential for the future of R&D in Israel. On this rare occasion when Israel was forced to choose between standing on the ideological principle of settlements or benefitting from the EU relationship, Israel chose the latter.²⁹

Labelling settlement products

The EU has an obligation to ensure the coherent application of EU consumer protection and labelling legislation to allow European consumers to make an informed choice when purchasing any products, including those from Israel or the settlements. However, many European retailers do not currently distinguish between Israeli and settlement products in their consumer labelling, and they are under no EU obligation to do so. The European Commission has therefore been working on EU-wide guidelines on the correct labelling of imported products originating beyond Israel's pre-1967 borders in order to clearly differentiate between settlement products, Palestinian products, and those originating within Israel.

But their issuing has been repeatedly deferred due to various political considerations, first as a desire to refrain from "rocking the boat" during US-led Israeli-Palestinian negotiations, and then in order to not be seen to be intervening in Israeli elections. In the absence of any

²⁸ Nikolov, "Ashton's Second hat".

²⁹ For more details on Israel's reaction to Horizon 2020 and the EU funding guidelines see this analysis from the Israeli think tank Molad, 11 August 2013, available at <http://www.molad.org/en/articles/New-EU-Guidelines-Israeli-Reception>.

diplomatic process, and with the new Israeli government now settled into office, a decision to issue labelling guidelines has apparently moved closer. Blockage at the EU level has not, however, stopped member states from pursuing their own national labelling policy. So far, three member states – the UK (2009), Denmark (2012), and Belgium (2014) – have introduced their own voluntary national guidelines.

While only three EU members have taken this minimal step, there does nevertheless seem to be a clear majority in support for such action at an EU level. Sixteen EU members (including the three above) in April 2015 publicly backed the introduction of EU-wide guidelines on the matter, citing the EU's May 2012 FAC commitment.³⁰ Their letter also showed a degree of exasperation that a vow made in July 2013 by then EU High Representative Catherine Ashton, following a previous call by 13 EU foreign ministers, that the EU would issue its own guidelines to this effect by the end of 2014 had still not materialised.

Business advisories

Some seventeen EU member states have also issued advisories warning businesses of the legal and financial consequences they could expose themselves to if they do business with entities linked to Israel's occupation.³¹ An advisory issued by the Spanish government in June 2014, for example, warned of potential disputes "over land, water, quarries, or natural resources that were acquired or invested in" and stressed that business activities in the settlements are liable "to lead to involvement in breaking international law".³² Following a similar advisory issued by the Dutch government, pension giant PGGM decided to divest from five Israeli banks, specifically over occupation-related concerns, with Luxembourg's general pension fund FDC following suit. In Denmark, Danske Bank sold its holdings in Israel's largest bank, Hapoalim, and blacklisted it. Most significant has been the decision of KLP Kapitalforvaltning, a major Norwegian insurance company, to divest from two international building material companies that own Israeli subsidiaries operating quarries in Area C of the West Bank – representing the first instance of "tertiary divestment".

Open questions about applying differentiation

As demonstrated by the case of the 2013 guidelines and the subsequent negotiation over Israel's inclusion in Horizon 2020, well-conceived and legally based differentiation can be effective in opening a discussion in Israeli society over the sustainability of the status quo in the OPTs and its effects on Israel's integration with Europe.

³⁰ The 16 member states are: France, Britain, Spain, Italy, Belgium, Sweden, Malta, Austria, Ireland, Portugal, Slovenia, Hungary, Finland, Denmark, the Netherlands, and Luxembourg. See Peter Beaumont, "Foreign ministers petition EU to urge labelling of settlement products", the Guardian, 16 April 2015, available at <http://www.theguardian.com/world/2015/apr/16/foreign-ministers-petition-eu-to-urge-labelling-of-settlement-products>.

³¹ Barak Ravid, "12 more EU countries warn against trade with Israeli settlements", Haaretz, 3 July 2014, available at <http://www.haaretz.com/news/diplomacy-defense/.premium-1.603030>.

³² Gianluca Mezzofiore, "BDS Scores Another Victory with Italy and Spain Warning Against Business in Israeli Settlements", International Business Times, 27 June 2014, available at <http://www.ibtimes.co.uk/bds-scores-another-victory-italy-spain-warning-against-business-israeli-settlements-1454446>.

In December 2013 ECFR conducted its "Two State Stress Test", aimed at assessing which factors were most responsible for undermining prospects for achieving a two-state outcome.³³ The evidence-based exercise showed how, along with the expansion of settlements and the physical entrenchment of the occupation, the other single factor most undermining the birth of a Palestinian state living peacefully alongside Israel was the dynamics of the Israeli debate where a majority is unwilling to move away from the status quo, either out of ideology or for lack of any sense of urgency. For this reason, further implementation should not be seen as an irritant but rather as a tool to impact what is one of the major obstacles to a negotiated solution of the conflict, namely the positions of the Israeli debate and the sense of impunity.

Moreover, both the EU and its member states now perceive differentiation between Israel and its activities in the OPTs as a logical consequence of the deep (and ever deepening) integration between Israel and the EU. To this end, there are several areas where the logic of differentiation calls for further consideration and legal analysis, both by the European Commission and by the governments of member states.

Integration between the European and Israeli financial sectors. The settlements are an important and integral part of Israel's financial sector, which provides mortgages, loans, and grants to local authorities within the settlements. Israeli banks also play a crucial role in financing the state-sponsored transfers of land, construction, and business activities that effectively create and sustain the settlements.

Through their banking transactions with Israeli banks and multinational corporations active in the OPTs, European banks could actually be increasing the supply of capital directed into Israeli settlement-related lending and investment. As the European Commission made clear in its guidelines on the funding of settlement entities in 2013, EU-funded and, by extension, member state-funded lending and investment may not be provided to Israeli entities operating in the OPTs. This is owing to the fungibility of the financial capital employed by all such corporate entities and the fact that all of their operations in the OPTs are established in contravention of international law. In this respect, both the European Commission and member state governments should investigate the following questions. Can the EU and member states permit themselves to supply fungible funds to European banks without ensuring that such funds cannot be directed into the capital structure of such Israeli entities? And, therefore, do day-to-day dealings between European and Israeli banks comply with the EU requirement not to provide material support to the occupation? Can European branches of Israeli banks be licensed to collect deposits and attract investments in the EU without ensuring that the fungible proceeds of these operations cannot be directed into the capital structure of such Israeli entities or employed to fund activities that contravene international law and are unlawful according to EU law? More generally,

³³ Mattia Toaldo, Fatima Ayub, Hugh Lovatt, and Dimi Reider, "Israel/Palestine – Two-State Stress Test", European Council on Foreign Relations, December 2013, available at http://www.ecfr.eu/page/-/ECFR_Two_State_Stress_Test_December_2013.pdf.

do investments in undifferentiated Israeli companies and institutions comply with the requirements of the EU's differentiation between Israel within its 1967 borders and Israeli entities in the OPTs?

Charitable status within the EU of organisations that support the settlements. Currently, a number of charities registered within the EU or its member states enjoy tax-exempt status even though they support Israel's settlement enterprise through their fundraising activities. According to charities such a status allows EU citizens to make tax-deductible donations that go towards supporting activities, services, and infrastructural investments in Israeli settlements which serve to consolidate them and promote their expansion. Given that the EU and its member states consider the settlements illegal, both the European Commission and EU member state governments should review whether support for these charities can be considered to be serving a charitable purpose under their own tax rules and charity regulations.

Validity in the EU and its member states of legal documents issued by Israeli authorities within the OPTs. The EU's non-recognition of Israeli sovereignty over the OPTs has been recently considered to imply the non-recognition of the competence of Israeli certifying authorities in the OPTs. It also implies the non-recognition of Israeli entities and institutions established in the OPTs, the legal basis of their acts, and the acts themselves. Therefore, the European Commission and EU member state governments should review the validity within their respective jurisdictions of certificates issued to Israeli nationals by Israeli entities established in the OPTs, or on the basis of Israel's application of its legislation to the OPTs.

Two initial cases arise when investigating this issue. First, should European institutions and employers recognise the certificates of educational qualifications issued by settlement entities, such as Ariel University or other settlement education establishments? Second, can property deeds derived from Israel's application of its national legislation to the OPTs or from acts of appropriation carried out by Israeli authorities in the OPTs (acts that are internationally considered unlawful) be recognised as valid within the EU and member states?

Cooperation with Israeli authorities and state entities located in occupied East Jerusalem. The EU, like the rest of the world, notably including the US, has been clear in its non-recognition of Israel's annexation of East Jerusalem and its view on the illegality of Israeli settlements in this part of the city. Since 1967, Europeans have with a few notable exceptions consistently implemented this non-recognition, thus avoiding, for instance, holding meetings with Israeli officials in this part of town or allowing activities to be conducted with Israeli state bodies in East Jerusalem.

It may be worth more carefully assessing when EU and member state adherence to these policies requires them to effectively refrain from recognising or cooperating with Israeli institutions, organisations, or companies by virtue of the extensive or critical nature of their operations in the occupied

part of the city, such as the national police headquarters, Ministry of Justice, and Ministry of Construction.

Implications for dual EU-Israeli nationals residing or conducting activities in the OPTs. Many Israeli nationals have a European passport, either because they were born in Europe and later migrated to Israel or because they are entitled by law to ask for a European passport by virtue of previous family ties to a given EU member state. Differentiation affects them as European nationals – to the extent that European law defines the status and consequences of their activities, economic transactions, employment, or residence in the OPTs – differently from Israeli law. In this respect, several specific questions arise, some of which reflect ongoing work by the European Commission.

First, can European authorities recognise contributory pension entitlements acquired through a beneficiary's employment by an Israeli operator established in the OPTs? For transactions requiring a proof of residency in Israel, can European authorities recognise a proof of residency in a settlement? Ultimately, the question arises of whether European authorities can recognise an Israeli national's status as a resident of the OPTs.

Conclusion

There is no European consensus on deploying leverage vis-à-vis Israel. The exception to this rule lies at the intersection where Europe's commitment to its own legal stipulations bumps up against Israeli political insistence on blurring any distinction between its own recognised sovereign territory and the OPTs. As EU–Israel ties have continued to thicken across a range of areas, Europe has belatedly sought to comply with its own policy of non-recognition of settlement activity. The combination of a Europe increasingly complying with its own legal duty to apply this distinction, a deepening of bilateral ties, and an Israel ever-more stridently blurring the Green Line and refuting European entreaties is becoming the most promising arena for a positive European role in impacting Israeli/Palestinian dynamics.

Stepping up differentiation is consistent with past EU statements and conducive to the EU's policy objectives on the MEPP. Some are attributing a growing interest in differentiation to frustration with the policies of Netanyahu; what should matter, however, is less the colour of any given Israeli government but rather the contradiction between its pursuit of "facts on the ground" and EU legislation. The extent to which the European Council is delaying implementation of the EU's differentiation policy over apparent "political considerations" is therefore difficult to justify.

Differentiation is a legal prerequisite for the EU in order to avoid violating its own laws. Whether in the form of international or EU law, the legal infrastructure for differentiation exists, with the European Commission funding guidelines and the Association Agreement being two important examples. The political mandate to pursue differentiation also exists within the numerous FAC declarations issued by the EU over recent years.

Just as importantly, differentiation is one of the few policies on which EU member states agree. While EU countries and institutions may differ for various reasons over the degree to which exceptionalism should prevail in indulging problematic Israeli policies, a policy of differentiation based on upholding the EU's own legal obligations represents the best means for consensus-based action, both domestically within national politics and on an EU level. Even members such as Germany or the Czech Republic – both considered more reflexively supportive of Israel – have shown themselves to be receptive to this approach.

There is no evidence that offering Israel more “carrots” as an incentive to strike a deal with the Palestinians, or that restricting differentiation for fear of being distanced from the peace process by Israel have produced any wins for Europe's stated policy goals. In fact, after four decades, Israel has become so bloated on EU carrots that those that remain are hardly appetising enough to coax it into an agreement with the Palestinians. One case in point is the deafening silence that greeted the EU's offer in December 2013 of a Special Privileged Partnership for Israel in the context of a final status agreement.³⁴ Hence the argument made by civil society groups both within and outside the OPTs that far bolder steps should be taken in response to Israeli policies. This is, in fact, the animating logic behind the BDS movement, itself gaining increasing attention and which calls for a comprehensive boycott of Israel with little distinction made between recognised sovereign Israel and the occupation.

BDS is an argument that European leaders have rejected to date, but this has not prevented Israeli leaders from misrepresenting differentiation as a boycott of Israel. The description of BDS activities as “anti-Semitism in modern garb”, to use Netanyahu's words, is becoming part of the mainstream discourse in Israel.³⁵ Israeli politicians have gone on to lump EU differentiation under the same banner: Israel's former Foreign Minister Avigdor Lieberman has compared potential EU guidelines on the labelling of settlement products to Nazis forcing Jews to wear yellow stars³⁶; former Finance Minister Yair Lapid called the same guidelines a “stain on the EU”³⁷; while Naftali Bennett – Israel's current minister of education – has described the EU's funding guidelines as “an economic terrorist attack”.³⁸

This trend will only get worse if it continues to go largely unchallenged and if Europe continues to fail to acknowledge, own, and actively defend a policy that is eminently reasonable and in no way tinged with anti-Jewish

animus. At the moment, only the Israeli rebuttal narrative really exists in the public domain, so Europe needs to put forward its own narrative on differentiation, distinguishing it from a boycott and countering the concerted campaign to misrepresent, distort, and sometimes simply prejudice European actions. EU embassies and delegations have already been active in countering these accusations, but the European political class must do more to explain and own such a differentiation policy.

Israeli public support for the settlements is somewhat fragile. A well-messaged differentiation push will produce mixed reactions for sure, but that is a vast improvement on the currently skewed state of play. An Israel that accommodates the EU's need to comply with its own legal requirements and obligations – either by creating its own clear differentiation or by ending the occupation and its settlements policies – would no longer face this issue in its relations with Europe. Europe should remember that it is Israel that has a difficult choice to make, not it. The cost of choosing the proliferation of settlements over the ability to conduct normal relations with Europe should be made clear to Israelis, with the implications ultimately left for them to decide.

Recommendations

Political ownership. Under its own regulations and principles, Europe cannot legally escape from its duty to differentiate between Israel and its activities in the OPTs. It is because of this that a de facto process of differentiation has been under way for some years. But the EU has not done enough to own this process by explaining it as the manifestation of an explicit EU policy of differentiation. Clearly naming this as such will also help the EU's political echelons to better defend this policy in the face of ever more forceful and not infrequently scurrilous Israeli attempts to push back. The term “differentiation” should be used in all EU statements, actively promoted by the high representative, and adopted by EU leaders themselves. EU foreign ministers should also refer to this policy of differentiation in their FAC conclusions and elaborate a common messaging strategy. “Differentiation” should always be used as a common term in order to counter attempts to conflate it with the Boycott, Divestment, and Sanctions (BDS) campaign movement or any other form of sanctions against Israel.

More coherent implementation of existing rules. Even under existing political constraints in Europe, this policy of differentiation should be rolled out more coherently and deepened across the ensemble of the EU's relations with Israel. The European Commission should task each of its directorates general with reviewing their existing interactions with Israel in order to assess whether they adequately differentiate between Israel proper and the settlements. This should also be done to evaluate how much day-to-day dealings have been brought into line with the EU's 2013 funding guidelines. Member states, too, should conduct their own reviews in order to bring their relations with Israel in line with EU norms. Differentiation should be implemented at the national level, as done by Germany

34 Foreign Affairs Council conclusions on the Middle East Peace Process, Brussels 16 December 2013, available at http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/EN/foraff/140097.pdf.

35 “Netanyahu: BDS ‘Anti-Semitism in Modern Garb’”, CBN News, 18 February 2014, available at <http://www.cbn.com/cbnnews/insideisrael/2014/February/Netanyahu-BDS-Anti-Semitism-in-Modern-Garb/>.

36 “FM compares labels on settler products to Nazi yellow star”, the Times of Israel, 17 April 2015, available at <http://www.timesofisrael.com/liberman-suggests-eu-slap-west-bank-products-with-nazi-yellow-star/>.

37 Jonathan Lis and JTA, “Lapid: Call for labeling of West Bank goods a ‘stain on the EU’”, Haaretz, 17 April 2015, available at <http://www.haaretz.com/news/diplomacy-defense/.premium-1.652347>.

38 Solomon Piotrkowsky, “Bennett: Economic peace Attack” [Hebrew], Arutz Sheva, 16 June 2013, available at <http://www.inn.co.il/News/News.aspx/259292>.

when issuing its own bid for R&D in which settlement-based entities were excluded.

Explaining to Israelis. The differentiation policy should be explained to Israelis, both to specific target audiences (political, business, union, academic leaders) and to the public at large in a clear, consistent, and unapologetic manner. This messaging would distinguish differentiation from BDS and explain the legal imperative driving differentiation as well as possible remedies for the problems arising from differentiation – a peace agreement/end of occupation or Israeli compliance with Europe’s non-recognition legal obligation in the absence of peace. It will be for Israelis and the Israeli political class to then debate the implications of Europe’s policy for their own decision-making, having clarified the incompatibility of settlements and the blurring of the Green Line with the ability to fully benefit from EU relations in a legal and trouble-free way.

Mainstreaming. European publics along with the European Parliament and member states’ parliaments have an important part to play in promoting differentiation. They should hold their own governments accountable over its deficient implementation. Just as importantly, though, differentiation is a model that applies not just to the EU but to other multilateral organisations governed by international law that deal with Israel, whether sub-regional groupings like Mercosur, or international bodies like FIFA.

Extending the use of business advisories. Seventeen EU states have already issued advisories warning businesses of the legal and financial consequences they could expose themselves to if they do business with entities linked to Israel’s occupation, including buying real estate or entities based there, or otherwise financing settlement-based companies or supplying related services. The EEAS and the remaining member states should publish similar business advisories. The EU and its member states should also: mainstream the content of the advisories across government bodies, including embassies and economic ministries; conduct proactive awareness raising among the private sector, starting with chambers of commerce but also the public sector and academia; activate national contact points for corporate social responsibility; and map domestic companies linked to settlements and reach out to them.

More rigorous application of differentiation. There are several areas where the logic of differentiation appears to call for additional measures or at least to demand further consideration or legal analysis. The European Commission and the EEAS, as well as member state governments, should undertake a systematic review of the implication of differentiation in these areas, and the European Parliament and member states’ parliaments should scrutinise the process to make sure that obligations are being fully implemented.

As explored earlier in the paper, the areas to be reviewed should include: the integration of the European and Israeli financial sectors, given the role of Israeli banks in supplying capital and services to settlements; the charitable status within the EU of organisations that support Israel’s

settlement enterprise; the validity within the EU of legal documents issued by Israeli authorities in the OPTs; EU interaction with Israeli state authorities based in occupied East Jerusalem; and the implications for dual EU-Israeli nationals of residing or conducting activities in the OPTs.

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