

INDEX UNIT

COMMITTEE ON JERUSALEM

19 DEC 1950

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RESTRICTED

Com./Jer/W.25  
25 June 1949

ENGLISH  
ORIGINAL: FRENCH

Economic Aspects of the Constitution of a "Free Zone"  
in the Jerusalem Area.

(Working paper prepared by the Secretariat)

When the "preliminary draft for an international regime for the Jerusalem area" was being prepared, the Committee on Jerusalem, in the course of the discussions, considered the possibility of constituting the Jerusalem area a "free zone". Within the framework of the last preliminary draft prepared by the Committee\*, which provides, inter alia, for the co-existence in the Jerusalem area of two zones - a Jewish zone and an Arab zone - separated by a demarcation line to be fixed (Article 2), this paper explains:

- I. the organization of such a free zone, and
- II. the advantages and disadvantages of this institution\*\*.

I. Working of a free zone in the Jerusalem area.

1. The outstanding feature of a free zone in the Jerusalem area would be its constitution on a territory politically subject to two sovereign States - the State of Israel and an Arab State - and, in certain respects, under the authority of the United Nations Administrator.

2. The two sovereign States would establish their customs round the frontiers of the Jerusalem area. Such withdrawal of the customs cordons beyond the boundaries of the area would thus involve the

\* Com.Jer./W.18

\*\* On "free zones" in general, see the Memorandum on the "Free Zones" of Upper Savoy and the Gex district.  
(Com.Jer./W.19)

disappearance of any customs cordon on the inner political frontier of the area (see sketch annexed).

3. To explain the working of the zone by means of concrete illustrations various cases must be studied:

Goods coming from Israel or the surrounding Arab State - Such goods would enter the market formed by the Jewish and Arab zones of the Jerusalem area without being subject to any Arab or Jewish customs duties or to any restriction as to quantity. Goods from the State of Israel, for instance, would cross the Jewish customs cordon without paying Jewish export duties, and would enter the Arab zone without paying Arab import duties. They would circulate freely in the two zones of the City, and of the area, and could be purchased by any inhabitant or resident, free of customs duty.

4. Goods from foreign countries - Goods consigned to Jerusalem arriving at Haifa, for instance, or at an Arab port would be sent "in transit" through the State of Israel or the Arab State, without being taxed on entry at Haifa or at another Arab port by the customs of the country concerned. They would then be carried in sealed wagons or lorries from the seaport to Jerusalem. They would not pay customs duties in the countries they passed through. The question whether only the surrounding States (Israel and the Arab State) would let products through "in transit", or whether the other Arab States would grant the same privilege for goods consigned to or from Jerusalem, would have to be studied.

5. Products manufactured in the Jerusalem area and exported abroad - Such goods would pass "in transit" through the surrounding States to the seaport, or to the country of destination, without paying any customs duty to the State of Israel or the surrounding Arab State.

6. Goods admitted free of customs duty and re-consigned to a surrounding country - It is obvious that goods admitted customs-free to the Jerusalem area, if re-exported to Israel or the surrounding Arab country, would have to pay the customs duty in

the State concerned. Thus an American lorry purchased duty-free in Jerusalem from an Arab by a Jew of Jerusalem would have, before it could be sold in Israel, to pay Israeli customs duty.

7. Various ways exist of paralysing the working of a free zone, such as the establishment of tolls, of indirect taxation, or of sanitary regulations, for instance, for foodstuffs. Very special attention should be paid to this question, so that the institution should not be crippled by such devices.

8. On the Jerusalem market goods would circulate and be sold freely. Two currencies would be legal tender: (1) the Israeli pound, which would be legal tender in the Israeli zone; (a) the currency of the Arab State, which would be legal tender in the Arab zone. However, it would be highly desirable for both currencies to be legal tender throughout the whole of the Jerusalem area, in order to facilitate business. It would probably be necessary to make this point clear in the regulations for the free zone.

## II. Advantages and Disadvantages of the Institution of a Free Zone for Jerusalem.

### A. For the Jerusalem area, and particularly the City of Jerusalem.

9. Products arriving in Jerusalem free of duty from Israel and the Arab State, or any other country in the world, would encounter such competition on the Jerusalem market that the cost of living in Jerusalem would be relatively low, compared with the neighbouring countries. From the Arab countries and Israel would come mainly foodstuffs (agricultural and animal produce), while from the countries of Europe and America would come manufactured goods. Amman, for instance, where goods from all over the world are to be found at very low prices, is an entrepôt and important clearing house for the Middle East. Jerusalem might grow prosperous for the same reasons, in fact even more so, since no customs duties

would be levied on imported goods.

10. As a result, it would exercise an attraction for the population of the surrounding countries, drawn by the low cost of living and the free trade atmosphere which would prevail in the City, and would encourage the development of trade and of various "services" which could radiate throughout the surrounding countries (transport companies, for instance, with headquarters in Jerusalem).

11. This influx of population would probably lead to a rise in the value of real estate (land and buildings).

12. Finally, the cost of living in Jerusalem would make conditions easier for tourists and pilgrims. It might increase their number, and encourage them to stay longer. This would be important for a city like Jerusalem, in view of its special position, particularly when one considers the high cost of living in Israel, which threatens to spread to the whole of the Jewish zone of Jerusalem and prove a material obstacle to tourist traffic and pilgrimages.

13. If Jerusalem became an important centre of trade and supply for the neighbouring countries, the enrichment of its inhabitants would be of direct benefit to the municipality ( or municipalities), which would thus acquire richer and more varied taxable resources, a most important matter for a city with heavy municipal expenses, and which had difficulty in balancing its budget.

14. One of the methods employed by modern States to paralyse the working of free zones has been the introduction, or more accurately, the repercussions of the introduction of exchange and currency control. Jerusalem, being subject to two sovereign States, would enjoy an exceptional position:

(a) Israel would only be able to apply restrictions on the use of foreign currency to Jewish importers of foreign goods;

(b) the Arab State, if it had an exchange control, could only

apply it to its own nationals.

As a matter of fact it is really very unlikely, in view of the profits which could be made by local importers, that the two States would manage to co-ordinate their currency policies. The result would be that the Jerusalem zone would not experience paralysing exchange control restrictions and could receive goods from the whole world.

15. Finally, the establishment of a free zone would ensure that the economic life of the Jerusalem area was sheltered from fluctuations in the economic situation of the two countries - from an economic crisis in Israel, or an agricultural crisis in the Arab State.

B. For the Surrounding States:

16. Theoretically the institution of a free zone would place such modern industries as might wish to establish themselves in the Jerusalem area in a difficult position. It would deprive them of the Jerusalem area market, as they would be unable to establish and develop themselves behind protective customs barriers, and would be faced with the competition of products from all over the world.

In point of fact, the population of the Jerusalem area would constitute for Jewish industries, for instance, only a fraction of the Jewish clientèle of Israel, for products manufactured in Jerusalem by such Jewish industries would enjoy a protected market in Israel (Israeli customs duties being exceptionally high).

On the other hand, it should be noted that Israeli industrial products manufactured in the Jewish zone of Jerusalem or in Israel, might not find customers among the Arabs of Jerusalem, because the Arabs would have the manufactured products of the whole world to choose from, and these would often be of better quality, and almost always less expensive, than Israeli products.

17. Transjordan would run the risk of finding in the free zone of Jerusalem a redoubtable rival to Amman, which has so far been one of the most important clearing-houses for western goods in the Middle East, and one of the most active centres of contraband.

18. It is probable that the Parliaments of Israel and of the Arab State, taking their stand on the principle of the equality of citizens before the law, would protest against the institution of a free zone in Jerusalem, which would confer on the inhabitants of the Jerusalem area a higher standard of existence and a relatively low cost of living.

19. For the State of Israel, the institution of such a free zone might be very important if the Arab States continue their ban on exports to Israel. The free zone of Jerusalem might become the "channel" through which Jerusalem would receive products from the Arab world in spite of the ban. This fact is particularly important when it is realised that, until the outbreak of hostilities, a large part of Palestine food supplies came from the surrounding Arab countries, particularly Syria, the Lebanon, Transjordan and Egypt.

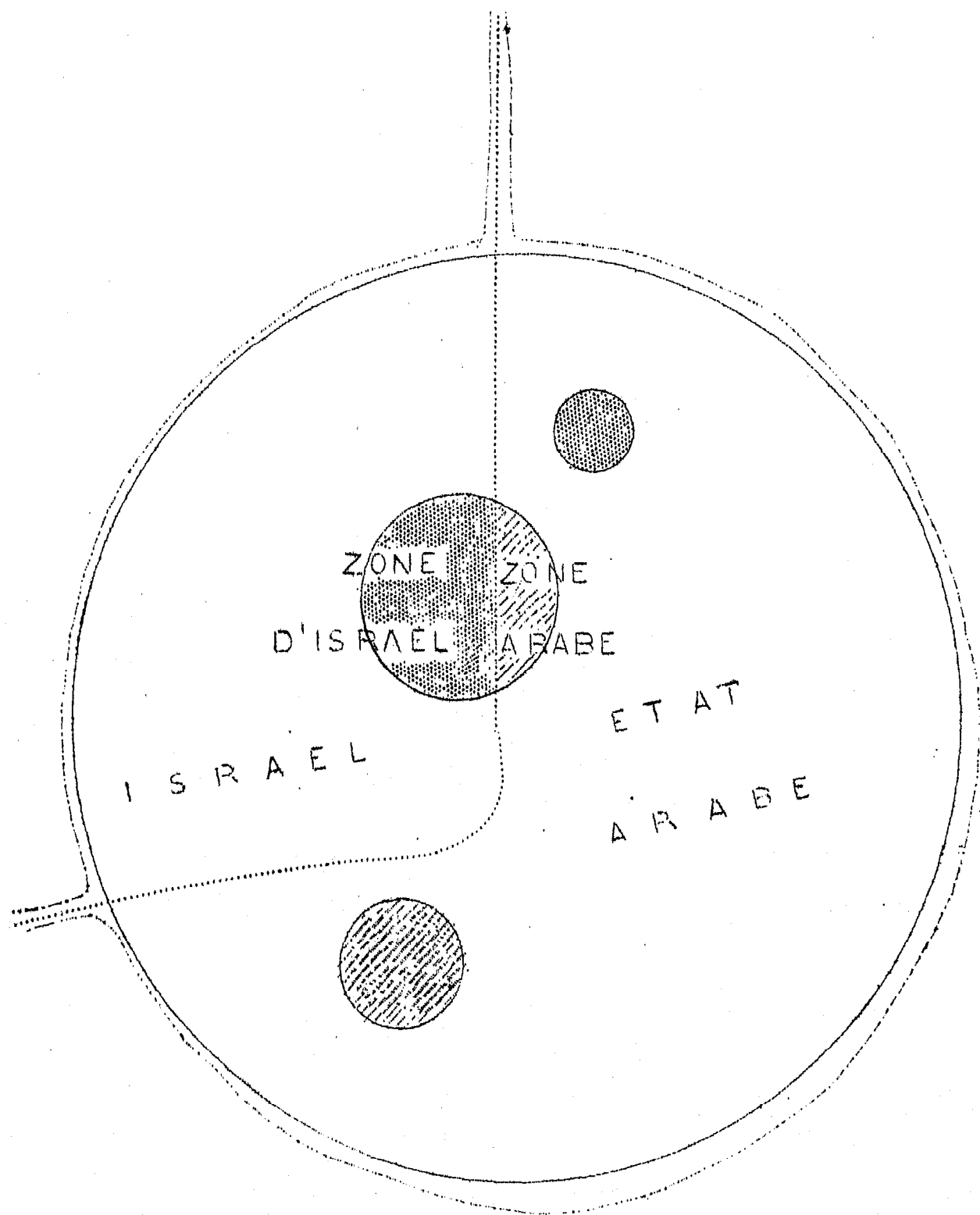
20. The cutting of a city into two zones, separated by a political frontier, is theoretically possible. From the economic point of view, it would lead to many and serious difficulties affecting the daily life of the citizens and tourists. Although the purpose of this working paper is not to analyse the consequences of such a division, these difficulties should be mentioned, if only briefly. The creation of a "free zone" would mitigate these difficulties for the economic life of a city and an area divided politically between two sovereign States.

21. The constitution of the Jerusalem area as a free zone of the kind described would give an economic basis to the area and, more

particularly, to the City which, though having its territory divided between two States, should retain a certain unity, and a certain international character.

The institution of a free zone would strengthen its unity, and create a community of interests in a city which, from the political point of view, would be distracted by opposing forces. It would develop a community of interests between Jewish and Arab citizens - a community of interests peculiar to Jerusalem which would enable the City to retain a relatively independent and international character.

SCHEMA D'UNE ZONE FRANCHE A JERUSALEM



..... FRONTIERE POLITIQUE.

----- CORDON DOUANIER ARABE

———— " " ISRAELIEN