



State Comptroller and Ombudsman
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Ministry of Finance

**State Balance
Sheet as of 31.12.18
- Investments
in Projects in
Collaboration with
the Private Sector**

Abstract

State Balance Sheet as of 31.12.18 - Investments in Projects in Collaboration with the Private Sector

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Background

Projects in partnership with the private sector (Public-Private Partnerships - PPP) are designed to provide infrastructure, products or services to the public through the private sector, utilizing the partners' relative advantage and through efficient allocation of risks and sources to derive value from them. In recent years, there has been a significant increase in the number of projects set up according to this model in various areas, amounting to tens of billions of shekels. The projects contributed greatly to the development of infrastructure in the center of the country and in the periphery.

Key figures

NIS **32.2** billion

The amount of the cumulative investment by the State in PPP projects (less depreciation) according to the Government's consolidated financial statements as of 31.12.18

27

The number of existing PPP projects as of the end of the audit, in the areas of transport (6), water (5), energy (3) and construction (13)

NIS **27** billion

The balance of outstanding financial commitments for the establishment and operation of PPP projects according to the government's consolidated financial statements as of 31.12.18

32

The number of PPP projects at various stages of construction and planning, as of the time of the audit, in the areas of transport (8), water (3), energy (2), construction (17) and environment (2)

NIS **60** billion






The expected investment scope in implementing PPP projects for infrastructure promotion in the coming years, according to the Accountant General's estimate


Audit Actions

 From February to September 2019, the State Comptroller's Office reviewed aspects related to investment management in projects in partnership with the private sector. The review was carried out in the Accountant General's Division of the Ministry of Finance - in the Infrastructure and Projects Division and in the Government Construction Administration; in Inbal - Insurance Company Ltd.; and in the Ministry of Defense. Supplementary examinations were carried out at the Bank of Israel, the Ministry of Finance's Department of Budget (Budget Department), the Capital Market, Insurance and Savings Authority (the Capital Market Authority), the Government Companies Authority, the Prime Minister's Office, the Ministry of Transport and Road Safety, the Ministry of the Interior, the Israel Police, the Water Authority and at TransIsrael Highway Ltd.

The Situation Reflected in the Audit Findings



-  **Lack of national investment strategy** - The government ministries, led by the Ministry of Finance, have not formulated a national investment strategy that includes prioritizing the various projects, which will support the government's ability to promote infrastructure that is essential for the country's economic growth.
-  **Lack of regulated collaborations and lack of consolidated knowledge** - The main bodies responsible for the management of state-owned contracts in PPP projects (contract managers) do not use standard tender documents and there is no standardized coordination between them in these matters, including with regard to the learning process, managing the timing of publication of tenders and outlining guidelines for conduct in the face of a conflict of interest. Such collaboration can reduce costs by utilizing economies of scale.
-  **Lack of full transparency in regard to ongoing government financial obligations** - Ongoing financial obligations for PPP projects in the amount of billions of NIS are not brought to the attention of all decision makers. Payments are spread out over a limited period relative to length of the contract, despite the importance of fiscal discipline for the entire period.
-  **Checking conformity for implementation of PPP based on unverified data and incorrect assumptions and without important components for such conformity tests** - Cumulative flaws have been found in conducting the adjustment tests that may bias their results, notably a lack of integrative assessments, a lack of sensitivity tests and international comparisons, use of unrelated streamlining coefficients and discount rates and the omission of transaction costs unique to PPP.
-  **Regulatory uncertainty** - The exemption of foreign banks from the obligation to receive a license, was established by a temporary directive (limited in time); this raises concerns that foreign countries' banks will be reluctant to grant credit to businesses in Israel, including investment in infrastructure in the framework of PPP projects.





 **Lack of a mechanism for weighing past experience** - It was found that the State did not formulate a mechanism that would weigh the past experience accumulated in working with the licensees, in a manner designed to deter unwanted behavior on their part in future projects and to increase the likelihood that they will meet schedules and budgets as undertaken.



Integrating the PPP model into a variety of projects - The use of the PPP model allows for the acceleration of the creation of projects incorporating cutting-edge private sector technologies, such as desalination facilities.

Formulation of National Infrastructure Projects List - The Prime Minister's Office promoted an initiative to formulate a list of future national infrastructure projects and made them available to international investors. However, the plan does not include all the required data, which could hamper fundraising from outside agencies to promote infrastructure, which is one of the government's goals.

Main Audit Recommendations

-  The Ministry of Finance - in collaboration with the various Government Ministries - must promote the formulation of a national investment strategy that includes priorities to support future economic growth. From it, the work plan for investment in PPP projects will be derived, and will be presented to the Government each year, including its budgetary implications.
-  The Minister of Finance must decide on the identity of the entity that will manage the engagement in PPP tenders by the State, and define the responsibilities and authority of the organizing body and the project manager.
-  The accompanying oversight team should promote the consolidation of knowledge accumulated in government entities through a mandatory implementation process for all government ministries, including the use of standard tender documents. The contract managers must also consider creating a uniform procedure that will be used by the whole government, which will include all the components that must be considered in conducting the conformity testing to check the best method for establishing and operating a project, including how to incorporate them according to the project being tested.
-  The Budget Department and the Accountant General's Office must consider applying rules to increase investment transparency, including how to present aggregate data of all of the outstanding financial obligations derived from all projects (determined by project flow and throughout the whole contract period), and the possibility of publishing investor returns while maintaining trade secrets, as is customary in other countries.

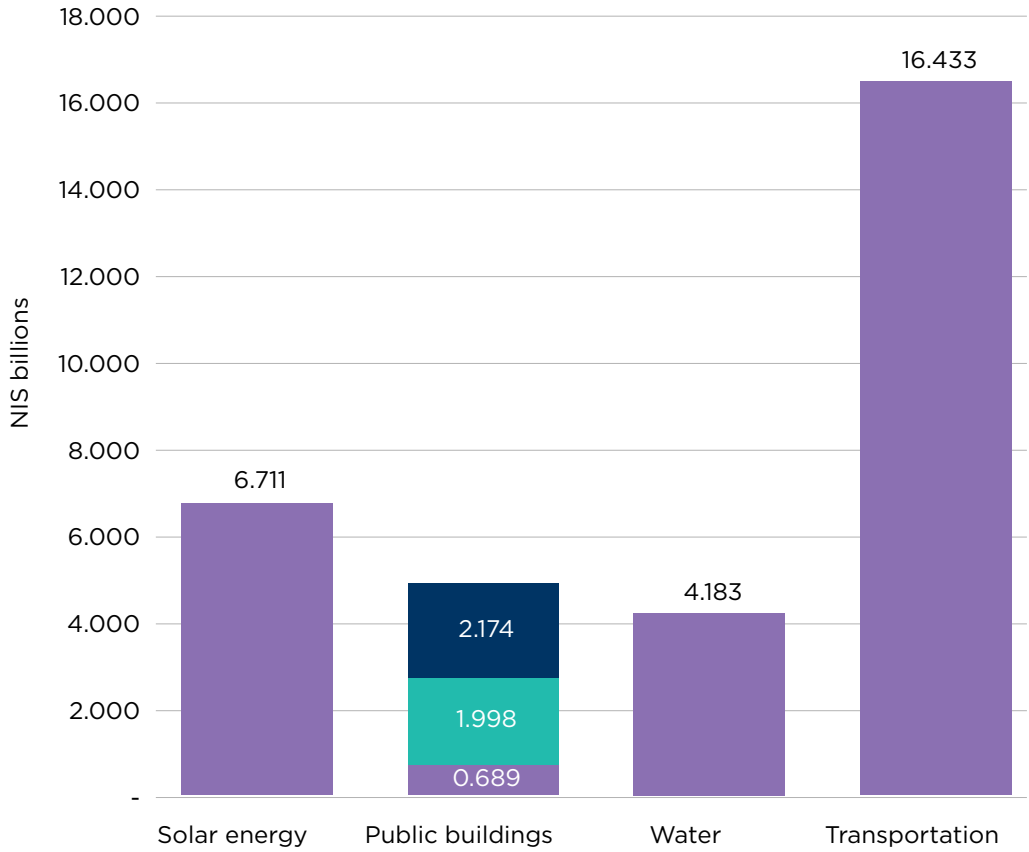


The Budget Department and the Accountant General's Office must examine the mix of capital sources of the partner sectors to finance PPP projects to reduce their cost, while ensuring continuous responsibility for project expenses throughout their operation. In addition, in view of the large volume of funds managed by institutional bodies, it is recommended that the Ministry of Finance examine the creation of tools to encourage investment in local infrastructure projects in order to enable benefit maximization for investors alongside contributing to the development of the economy.

Summary

Projects in partnership with the private sectors are of great importance in promoting state infrastructure in various fields. The findings that emerged in the report indicate the need to decide who will function as coordinator at the government level in order to realize maximum benefits at the national level and to improve the activities of the bodies responsible for such projects and undertakings. Establishing standardized working principles for carrying out projects in this model will enable investment in infrastructure projects to be increased while creating diverse investment channels in the economy and assisting the country's economic growth over the years. Formalizing steps to ensure that the outline is implemented after properly examining the benefits of engagement in relation to possible alternatives will result in maximizing the partners' relative advantages and efficient allocation of risks and resources. It will also ensure that the return on public capital invested in implementing these projects is maximized.

Investment in projects in partnership with private sectors as of 31.12.18, according to the operating body distributed by sectors



- Infrastructure and Projects Division
- Construction Administration
- Ministry of Defense

According to the government's consolidated financial statements for 2018, adapted by the State

