Office of the State Comptroller
Annual Report 71A | 2020

Issues of Broad Importance

Supervision and Monitoring of Statutory Corporations

Abstract

Part A – Supervision and Monitoring of Statutory Corporations

Abstract

Background

A statutory corporation is an independent body, established by legislation, that operates in the public sector. It has characteristics of both a government ministry and a government company as well as unique characteristics. It promotes public affairs in in accordance with its enabling legislation. In its role as a public trustee, it has legal obligations. It is charged with achieving the objectives defined for it in the enabling legislation. It has its own budget. Many of the statutory corporations receive funding from the State. Statutory corporations engage in a wide spectrum of public activities, including culture and sport, sanitation, archeology, safety, insurance, health and regional development. Some of these corporations engage in the provision of technical services to industry, transportation, employment and communications, while other corporations engage in regulatory activities.

Key figures

54
number of statutory corporations

15,000
number of employees in all statutory corporations

ILS 300 billion
volume of assets owned by all statutory corporations

ILS 100 billion
estimated annual income of all statutory corporations

22
Areas of activity in statutory corporations

0
statutory corporations that adopted the regulations of section 404 of the Sarbanes-Oxley Act (SOX)

73%
percentage of statutory corporations that do not make full financial statements available to the public

55%
percentage of statutory corporations whose board of directors is understaffed

Audit actions

From December 2018 to June 2020, the Office of the State Comptroller audited aspects relating to government supervision of the statutory corporations and their corporate governance. The audit findings relating to all statutory corporations are specified in Part A of the report. Part B of the report presents detailed audit findings regarding five major statutory corporations: the Standards Institution of Israel; the Israel Nature and Parks Authority; the Israel Sports Betting Board; Magen David Adom (the national emergency medical services organization); and the Israel Airports Authority. Follow-up audits were conducted in Magen David Adom and in the Airports Authority. Supplementary information was collected from the Ministry of Justice, the Prime Minister's Office, the Ministry of Environmental Protection, the Ministry of Finance (in the Commissioner of Wages Department and in the Accountant-General's Department), the Government Companies Authority and in the Ministry of Culture and Sport.

In January 2019, the Office of the State Comptroller distributed an online questionnaire to 48 statutory corporations regarding corporate governance issues and 31 corporations responded. The purpose of the questionnaire was to obtain a status report on the situation in the statutory corporations as of 1.12.18, a randomly selected date. The Office of the State Comptroller also examined select sections of the enabling legislation that established 15 major statutory corporations. The data presented below are based on the responses of 31 corporations to the questionnaire.

Key findings

- **Boards of directors composition:** the boards of directors of approximately 55% of the surveyed statutory corporations operated did not have a full complement of directors. Government agencies did not appoint civil service directors to the boards of nine of the 31 corporations surveyed (approximately 30%) as required by the enabling legislation. An examination of the enabling legislation of the 15 major statutory corporations revealed that for six corporations the number of directors need for a quorum to convene board meetings has not established. The maximum number of directors in these corporations ranged between 7 and 35.

- **Directors possessing accounting and financial expertise:** eleven of 26 corporations responding to the questionnaire (about 40%) do not have a director possessing accounting and financial expertise.

- **Management's responsibility for the accuracy of the data in the corporations' financial statements:** it was found that in four of the five large surveyed statutory corporations, the managers are not filing a declaration of personal responsibility for the accuracy of financial statements. They are also not filing an additional report of the effectiveness of the internal control, thereby failing to meet the accepted Israeli and international standards of corporate governance in government companies and in other companies.

- **Accountability of the internal auditor:** only in six out of the 25 corporations that responded to the question in this regard (about 25%), is the internal auditor accountable to the audit committee or to a similar board committee, while in the rest of the corporations (about 75%), the internal auditor is accountable to the chairman of the board or to the CEO.

- **Duration of incumbency of the CEO, legal advisor and independent auditor:** A review the laws establishing the 15 major statutory corporations indicated that six laws (40%) don't limit the CEO's term of service. The remaining laws limit the CEO's incumbency to eight to ten years. The audit found that in three out of 30 statutory corporations (10%), the CEO has been holding his position for 12 or more years. Additionally, in 13 out of the 25 corporations (10 of which are small corporations) that responded to the question in this regard (about 50%), external legal advisors have been retained for more than eight consecutive years. Additionally, in 10 out of the 25 corporations (40%), the independent auditor has been holding his position for ten or more years.

- **Transparency:** examination of the corporations' websites showed that only four out of the 15 major statutory corporations (27%) publish full financial statements. It was further found that three other corporations publish only highlights of their financial statements.

- **Risk management:** six out of the 26 corporations that responded to the question in this regard (about 23%) reported that they did not conduct a risk survey in 2016 – 2018. Only two out of those 26 corporations appointed a board committee for risk management.

- **Code of ethics and the prevention of conflicts of interest:** only six of the 15 major corporations surveyed (40%) published a code of ethics on their website. Nine of the 31 corporations responding to the questionnaire (about 30%) have no procedure for preventing conflicts of interest. Thirteen of the corporations (about 43%) have no procedure regulating the receipt of gifts and benefits, and only nine of them (30%) have a procedure requiring managers and directors to declare any conflicts of interest prior to taking office and during their incumbencies.

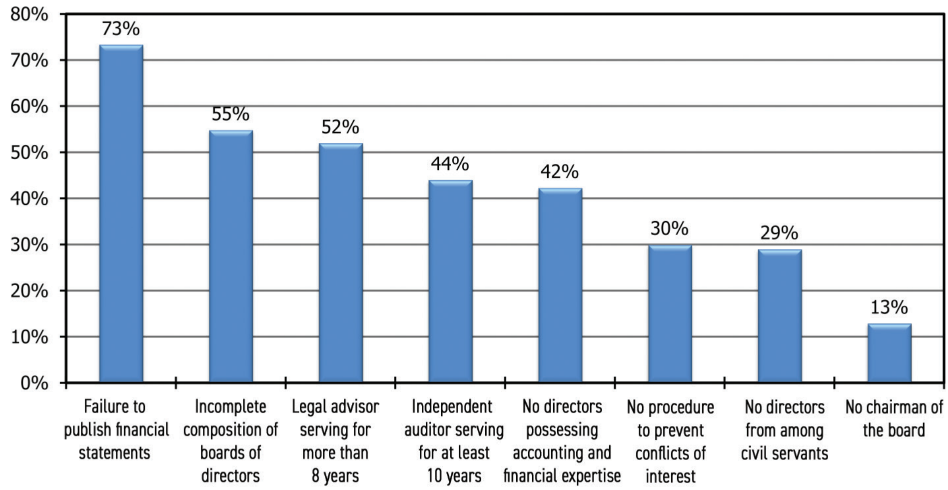
Appointment of an audit committee: although the vast majority of the laws establishing statutory corporations do not define an obligation to appoint an audit committee, according to the questionnaire distributed among the corporations, 27 out of the 31 corporations that responded to the questionnaire have appointed an audit committee.

Code of ethics in the Sports Betting Board (Toto) and in the Standards Institution of Israel: the Sports Betting Board has adopted an international code of ethics for organizations in the sports betting sector, and it retains an external advisor to conduct an annual examination of compliance with the code of ethics by the Board's employees and its concessionaires. The Standards Institution ratified the executive committee's code of ethics as a result of the audit.

Key recommendations

- It is recommended that the Ministry of Justice, the Prime Minister's Office and the Ministry of Finance should take action to examine ways to ensure that boards of directors operate with a full complement of directors as is required.
- It is recommended that each corporation should examine the need to appoint at least one director possessing accounting and financial expertise in order to improve the board of directors' work and the corporation's financial and accounting control.
- It is recommended that the statutory corporations, particularly those with annual revenue or assets exceeding ILS 400 million, should consider the possibility of applying rules regarding managerial certification of the financial statements' accuracy (pursuant to SOX 302) and the possibility of adopting the rules regarding comprehensive examination of the effectiveness of the internal control (pursuant to SOX 404) and that the relevant government ministries should consider issuing a directive in this regard.
- It is recommended that all statutory corporations should publish budgetary data, work plans and updates on stages of their implementation on their websites.
- It is recommended that all statutory corporations should complete the drafting of a code of ethics and should publish it on their websites, and that they should complete the preparation of compulsory procedures to prevent conflicts of interest. It is also recommended that the Ministry of Justice, the Prime Minister's Office and the Ministry of Finance should consider drafting a generic code of ethics specifying all rules of conduct for employees and directors in the statutory corporations, while enabling customization of the code of ethics to the corporation's unique activities.
- It is recommended that the Ministry of Justice, in collaboration with the Prime Minister's Office and the Ministry of Finance, should take action to comprehensively regulate statutory corporations' activities and should consider the possibility of appointing a government authority to be delegated with the sole responsibility for all statutory corporations and the supervision over them, while corporations of a regulatory nature maintain their independence. It is further recommended to prepare and publish a best practice guide, and to augment the supervision and control over all statutory corporations.

Percentage of corporations with various deficiencies in corporation governance*



Source: summary of the data appearing in this report.

* The percentage of deficiencies in each topic relates to the findings of the relevant sampling prepared for the topic.

Summary

On the audit completion date, every statutory corporation is operating pursuant to the law that established it, but no government authority has been delegated sole responsibility for supervising all statutory corporations and for considering innovative and technologically advanced supervisory methods; no actions are being taken to comprehensively regulate matters pertaining to all statutory corporations.

Some of the main auditees (the Prime Minister's Office, the Ministry of Justice, the Government Companies Authority, the Ministry of Culture and Sport and the Airports Authority) have stated that they attribute considerable importance to the audit report and its findings on the subject of the supervision and monitoring of statutory corporations and the need to strengthen the corporate governance in them.

Based on the findings of this audit of corporate governance in statutory corporations, it is proposed that the Ministry of Justice, in collaboration with the Prime Minister's Office and the Ministry of Finance, should take action to comprehensively regulate all statutory corporations, and should consider the possibility of appointing a single government authority to be delegated the responsibility for all statutory corporations and the supervision over them, while corporations of a regulatory nature maintain their independence. It is further recommended to prepare and publish a best practice guide to augment the supervision and monitoring of statutory corporations.