



Office of the State Comptroller  
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Government Water and  
Sewage Authority

**Water and Sewage  
Corporations  
– Regulation,  
Management and  
Supervision**

Abstract



# Water and Sewage Corporations – Regulation, Management and Supervision

## Abstract

### Background

In 2001, the Water and Sewage Corporations Law was enacted. It transferred the management of the water and sewage systems from the local authorities to water and sewage corporations. The law sought to ensure proper standards of service, professional efficient business management and the utilize revenues for investments in water and sewage infrastructures (hereinafter – the incorporation reform). Until the beginning of 2020, 56 corporations were formed that included 158 local authorities that were obligated to incorporate<sup>1</sup>; 24 local authorities that were obligated to incorporate have not yet done so. Attempts have been made since 2006 to establish regional corporations to consolidate the number of corporations and increase their service areas. At the audit completion date in December 2019, the proposed formats for regional incorporation have been unsuccessful.

### Key figures

#### ILS 4.6 billion

the volume of revenues of the water and sewage corporations in 2018. Total profit in 2018 was ILS 273 million

#### 45%

of the average uniform tariff to household consumers for 2019 constitutes the corporations' cost component (ILS 9.059 per m<sup>3</sup>)

#### 60%

of the benefits budget allocated for populations entitled to a discount off their water bills in 2015-2019 was not utilized (ILS 153 million)

#### ILS 8.6 billion

the corporations' total investments in water and sewage infrastructure in 2011-2018

#### 43%

of the volume of the grants given to local authorities and to corporations in 2007-2016 <sup>2</sup> in order to incentivize incorporation and regional incorporation and to help during the initial incorporation period was not utilized – about ILS 940 million, out of ILS 2.2 billion

#### 56 corporations

exist on the audit completion date. These corporations provide service to about 95% of the population of those local authorities required to incorporate by law, although at this time, the maximum number of corporations by law is supposed to be 30


1 Additionally, two local authorities incorporated that were not required to incorporate.

2 The grants were paid up until 2018.

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## Audit actions

 From May to December 2019, the Office of the State Comptroller audited various aspects of the water and sewage corporations, including an examination of the success of the incorporation reform and an examination of the fulfillment of the objectives defined in the Water and Sewage Corporations Law. The mechanism of benefits to disadvantaged populations was also examined. The audit was conducted in the Water Authority and in several water and sewage corporations with differing characteristics, including population size, number of authorities holding the corporation, the average socio-economic rank of the population and sectors.

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## Key findings

-  **The water tariff to household consumers** – in 2010, as a result of the tariff reform<sup>3</sup>, the water component of the water and sewage tariffs (i.e., excluding the sewage tariff) increased by 30%. Subsequently, the tariffs were lowered until July 2018, followed by a moderate increase until January 2020.
-  **Partial reduction in the water loss ratio**<sup>4</sup> – from 2011 to 2018, the average water loss ratio improved. The savings was achieved due to the decrease in the average water loss during the years 2011–2018. The annual savings in 2018 was approximately 29 million m<sup>3</sup> worth roughly ILS 203 million. Nevertheless, in 2018, the actual average water loss ratio (9.64%) was still higher than the average water loss ratio defined by the Water Authority (7.97%). The annual gap totals about 10 million m<sup>3</sup> and equivalent to an annual financial loss of about ILS 69 million. The highest gap was recorded in corporations defined as entitled corporations that serve minority populations<sup>5</sup>. Consequently, one of the main goals of the incorporation reform has not been fully achieved.

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3 The Water Authority Council was responsible for the water tariff reform. With this reform, the Council changed the mode of calculation of the water tariffs and based them, inter alia, on the principle of the recognized cost, on discontinuing the government subsidy and on imposing all of the costs on consumers, including water desalination costs and higher sewage treatment costs for the purpose of achieving better quality treated waste water. It should be noted that the tariffs that the Authority defines since 2010 includes a sewage component, while previously, the sewage fees were set according to municipal bylaws.

4 Water loss is the difference between the volume of water purchased (or produced) and introduced into the water system and the volume of water that consumers are billed. Water loss can derive, for example, from faulty water meters, from trickling, from water leaks and from water theft.


5 These corporations were classified as “entitled corporations” for grants and for more lenient norms. “Entitled corporations” were defined as weak corporations with particularly high water loss ratios that are incapable of independent financial subsistence during their initial years of operation and are eligible for grants and more lenient norms.



- ❗ **Partial reduction of the collection loss ratio** <sup>6</sup> – among the corporations examined, an average decrease was found in the current collection loss ratio in 2011 compared to the ratio in 2018. The average current collection loss ratio in 2018 among the entitled corporations (28%) was significantly higher than that ratio among the rest of the corporations (11%). Even after two years of collection efforts, the gaps are still significant. Thus, the cumulative average collection loss ratios as of December 2018 for billing in 2016 among the entitled corporations (13%) was higher than that ratio among the rest of the corporations (3%) and fails to achieve the norm defined by the Authority for the weak corporations – an average ratio of about 3%.
- ❗ **Significant differences between the corporations** – there are significant differences between the entitled corporations and the rest of the corporations. Although the entitled corporations received financial assistance through a cross-subsidy in tariffs and grants so that they will be capable of achieving the norms defined by the Water Authority, correct to 2018, this objective has not been achieved. The differences were found in all operation aspects: profitability, financial robustness, water loss, investments and collection losses.
- ❗ **The corporations' accounting control and supervision tools** – the accounting control and supervision tools that the Water Authority required the water and sewage corporations to implement were found to be deficient. The process that the Water Authority instituted in 2017 to regulate this issue was discontinued, even though a decision had been made to continue it in another format. The possibility of continuing it through an alternative procedure was not considered.
- ❗ **Implementation of compulsory regional incorporation** – the government policy since 2006 has been, inter alia, to encourage regional incorporation, which was supposed to reduce the number of corporations. Compulsory regional incorporation has been anchored in law since 2013. Nevertheless, on the audit completion date, the number of corporations has not been reduced. Local authorities with a low socio-economic rank established mainly low rank corporations<sup>7</sup> ranked low on the socio-economic index. The format of regional incorporation that the Authority proposed in 2013 and in 2019 was not implemented, despite the incentives and grants offered by the Water Authority to encourage regional incorporation. Only 24 of the current 56 corporations are serving more than 100,000 residents each.

6 Collection loss is calculated as a ratio of uncollected billing out of an issuing corporation's total billing. The Office of the State Comptroller examined the corporations' current annual collection loss values in 2011 compared to 2018 as on each December 31. It should be noted that the calculation of the current loss as on December 31 of each year did not take into account revenues from billing collections subsequent to the end of the year, such as billing not yet due on December 31 and collections from enforcement actions received after the end of the year.

7 The social economic rank of the corporation is derived from the average rank of the local authorities that the corporation serves.

 **The assistance mechanism to disadvantaged populations** – the assistance mechanism to disadvantaged populations is not leading to full utilization of the benefit allocated for this purpose. Two and a half years have elapsed since the date the Knesset Finance Committee issued a directive to prepare a new model for providing assistance to disadvantaged populations. The directive aimed to amend the regulations. The Water Authority forwarded a proposal for a new model and amendments to the regulations to the Ministry of Finance May 2017. Nevertheless the Ministry of Finance has not yet submitted a draft amendment to the regulations to the Finance Committee and the assistance mechanism has remained unchanged. It should be noted that about 60% of the assistance available to the customers eligible for a discount on their water bills in 2015-2019 was not utilized (ILS 153 million).




**The corporations' profitability from 2011 to 2018** – the corporations' profitability improved between 2011 and 2018. In 2011, there were 52 corporations operating and their total profit was about ILS 10 million which reflected a negligible annual return and 58% of the corporations ended 2011 with a loss. In contrast, the corporations' total profit in 2018 was estimated to be approximately ILS 273 million, reflecting an annual return of about 6%. This is the customary return for the controlled infrastructure service sector – which is a monopoly. 18% of the corporations ended 2018 with a loss.

**Corporate investments** – during the years 2011 – 2018 the corporations invested ILS 8.6 billion in the water and sewage systems including ILS 1.3 billion in 2018. Additional sums were invested in sewage treatment plants.

**Using water disconnections as a collection tool from household consumers** – the promulgation of rules regarding water disconnections in 2015 by the Water Authority Council and its activities to implement these rules almost completely eliminated the practice of corporations using water disconnections as a means to collect household consumers' current debts.

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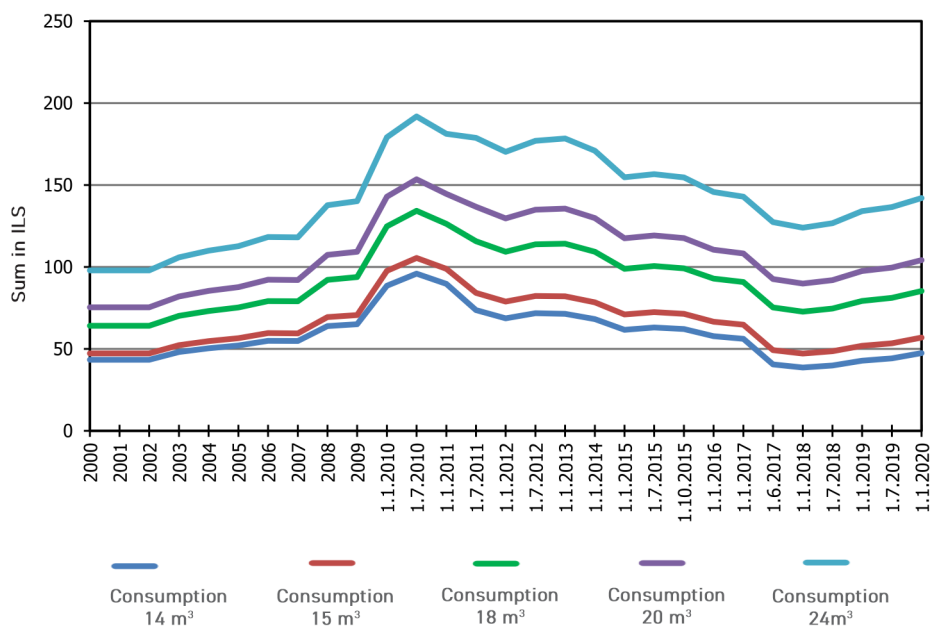
## Key recommendations

 It is advisable to consider ways to ensure the financial robustness of the entitled corporations ranking low on the socio-economic index, of corporations with a low profit margin and those recording losses, in order to ensure that they comply with the norms stipulated for them. It is also recommended to consider offering grants in the future that will be contingent upon meeting clear targets regarding required infrastructure improvements and compliance with norms that define milestones and measurable interim targets. These yardsticks will enable supervision and monitoring grant fund usage.



- 💡 Consumers' payments for water and sewage services are intended as a financing source. In light of high annual and cumulative losses due to collection losses, the Water Authority and the corporations, particularly the entitled corporations, should monitor debt collection and consider additional ways to improve the collection ratio. These steps include utilizing additional collection methods and mapping of additional governmental entities outside of the water system that could assist them to achieve significant improvement as well as meeting the normative collection loss norm.
- 💡 It is recommended that the Water Authority focus on corporations deviating from the water loss norm and take action so that the corporations formulate a plan for achieving the required norm. as, The Water Authority should develop mechanisms to encourage corporations to streamline and maximize profit. It is also recommended that the Water Authority should consider the corporations' infrastructure investment plans according to the expected growth in population.
- 💡 The Water Authority should take action to regulate internal control in the water and sewage corporations, and consider raising the topic for discussion by the Water Authority Council, which has the authority to set rules that will apply to all of the corporations.
- 💡 It is recommended that the Water Authority submit a proposal to the Water Authority Council to amend the service criteria so that they will contain detailed regulations regarding the publication of consumer inquiries to the corporations in order to create reporting uniformity. Inter alia, it is advisable that the Water Authority Council should also consider adding a requirement that the corporations report data to their consumers about increased consumption and the handling time of public inquiries. This will increase transparency regarding relevant consumer information.
- 💡 Considering the low utilization ratio of the benefits by entitled consumers and considering the Knesset Finance Committee's directive, it is advisable that the Ministry of Finance, which is responsible for preparing regulation amendments, and the Water Authority, as the regulatory authority and the supervisor of the water system, take action to revise the assistance mechanism to the entitled populations in a manner enabling optimal benefit utilization.
- 💡 In order to implement mandatory regional incorporation, the Ministry of Finance, the Water Authority, the local authorities and the Federation of Local Authorities should analyze all governance, financial, cultural and topographical considerations. This will assist them in devising a solution to overcome the problems regarding the poor condition of the infrastructure, and the high water loss and collection loss ratios in authorities with a low socio-economic ranking. The resulting regional incorporation plan that shall be proposed, should be used while seeking solutions for these issues.

## Water bills for household consumption (without the sewage component) 2000 – 2020 (at real prices)



According to data from the Water Authority, processed by the Office of the State Comptroller.

## Summary

The objectives of the incorporation reform, which transferred the management of the water and sewage system to water and sewage corporations, were partially achieved. Although there was some improvement in the corporations' operating indicators and most of the local authorities incorporated, there are still gaps compared to the norm, and the regional incorporation format was not implemented. Along with actions to promote regional incorporation, which is part of the spectrum of actions needed to advance the reform's objectives, additional actions should be considered, including contending with the unique issues facing the entitled corporations and the disadvantaged populations, weak internal controls and increasing collection losses. Additionally, the provisions of the law regarding regional incorporation and reducing the number of corporations should be implemented and actions should be taken to streamline the corporations, inter alia, by narrowing the gaps between the actual costs and the normative costs defined by the Water Authority.