



State of Israel

State Comptroller  
and Ombudsman of Israel

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Annual Audit Report  
72a – Part Two | 2021

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Abstracts



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## Foreword

**The 72a Annual Audit Report – Part Two**, submitted to the Knesset, is the second part of the State Comptroller's annual report presenting audit findings on the audited bodies for 2020. The report contains audits regarding national infrastructures and economy, areas that are essential keystones for the development of the economy and for improving the quality of life in Israel.

Over the years, the State Comptroller's office has given special emphasis on auditing systemic issues with broad national effect. This report includes findings raised in systemic audits regarding the following issues: National programs for developing the north of Israel; Investment management at various entities and in Mifal Hapayis (the national lottery of Israel). Following is a short overview of these audits:

The population in Israel's northern district, as of 2019, totaled 1.5 million residents, constituting 16% of the total population in Israel; there are 424 settlements in the northern district, and its area covers 4,473 square kilometer. The audit regarding **the national programs for developing the north of Israel** raised that in 2016 the government decided on formulating a strategic multi-year program for developing the northern district and presented it in 2017. A budget of NIS 17.3 billion was allocated for the implementation of the program. The audit found that some of the obstacles the northern district faces in various aspects preventing an optimal implementation of the projects included in the government decision, were not examined, and therefore the preference given to the northern district was not effective. Some of the allocated budgets for the national program were not fully utilized, and objectives set in the government's decision were not achieved. In addition, the audit found that the strategic steps for financial development in the mid-range in the northern district, which could lead to the necessary change in the northern district in all aspects of life, were not sufficiently promoted. For example, as of the audit concluding date only NIS 37.5 million of the NIS 400 million allocated in accordance with the government decision for projects recognized as "national ventures" were utilized. In terms of current poverty levels and disparities between the northern district and other districts in various areas, including employment and salaries, education, higher education and health, the audit found that since the government decision was made there has not been a significant improvement in these disparities, and the northern district is staged lower compared to all other districts in most of the examined parameters. For example, in 2018 the number of hospital beds in the northern district was 1.5 per 1000 capita, the lowest rate of all districts. It is recommended that the government ministries review the situation of the northern district compared to other districts and the effectiveness of the actions included in the government decision in order to promote a follow-up program to narrow the gaps between the northern district and all other districts and ensure the provision of appropriate and ongoing services to all the residents of Israel.





In the chapter dealing with **investments management at various entities** the audit found that as of 30.6.20 the value of ongoing investments of the audited institutional bodies, government companies and statutory corporations totaled NIS 9.4 billion of which NIS 6.4 billion are designated for pensions; the value of long term investments made by the audited local authorities totaled NIS 4.9 billion. The audit found deficiencies in the administrative and professional aspects of investments committees' activities in the audited entities. In times of crisis, where fluctuations on the capital markets can erode the investments portfolios, it is highly important to increase the supervision and control on investments in these entities, inter alia through the investments committees and through educated risk management. The performance of an educated investment management by local authorities and public sector entities – including determination of a suitable investment policy taking into account considerations of financial gain or maintaining the real value of the investment, investment periods and risks – will maximize the inherent benefits of the funds held by the entity.

The commitment of the society in Israel to ensure the rights of persons with disabilities is based on acknowledgement of the principle of equality, of the value of every human being and in human dignity. Public transportation is essential for persons with disabilities, providing them with independence and access to employment, education and health services, and allowing them to pursue community life and integrate into the society. This report includes a chapter on the subject of **providing accessibility in public transportation to persons with disabilities**. According to the Central Bureau of Statistics, the number of persons with disabilities in Israel in 2019 totaled 1.56 million (of which 1.2 million are age 20 and over); 50% of the number of persons with disabilities are unemployed; 33% travel daily using city busses compared to only 15% that travel by intercity busses. Many have to deal with low incomes (75% are persons with severe disability and with difficulties in financing monthly expenses (19% of persons with severe disability and 11% of persons with moderate disability), in maintaining a car (63%) and in obtaining a driver's license (60%). In addition to these difficulties, it is complicated for persons with disabilities to use the transportation they need in order to travel independently. Adapting the physical and human environment to the motorical, sensory, emotional and cognitive abilities of persons with disabilities is consistent with the principles of ensuring equal rights for persons with disabilities. This adaptation will enable them to live independent, respectable and equal lives in the community. Improving the ways of transportation for persons with disabilities will increase the opportunities for receiving essential services, provide new employment possibilities, and increase employment productivity. In addition, this improvement will reduce of the need for special transportation, resulting budget savings and financial benefits. Taking care of the weak is not only important for its contribution to individuals, but also for its contribution to society as a whole, in terms of values and moral standards. This a test as to the moral resilience of the society, being the foundation for its existence.

Yad Vashem – The World Holocaust Remembrance Center (Yad Vashem) is a public corporation. Its role is, inter alia, "to gather to the homeland the memory of all members of





the Jewish nation who perished under and fought and rebelled against the Nazi enemy and their collaborators and to commemorate them, their communities, organizations and institutions destroyed because of belonging to the Jewish nation, and to commemorate the righteous among the nations". The Yad Vashem complex is spread over 180 dunams on Memorial Mount in Jerusalem, and its ongoing budget the years 2017–2019 was NIS 200 million. Its annual deficit for 2020 was NIS 25.6 million. In the chapter dealing with **aspects in the activities of Yad Vashem – The World Holocaust Remembrance Center** it was shown that Yad Vashem holds large collection of objects and documents with unique historical value designed to assist in commemorating the holocaust, and which require improvement in their management to ensure their preservation for the coming generations. In order to do so, Yad Vashem should improve its recording and cataloging of the items; should computerize the preservation activities and operate to complete them before the condition of the items deteriorates; should verify adhering to standards of temperature, humidity and lighting in compatibility with updated museum standards. Yad Vashem should examine the annual deficit from its ongoing activities, and take action to balance the annual budget.

Ground water are a primary strategic source of water: half of amount of drinking water provided to the population and 40% of water for agriculture derive from ground water. In Israel, ground water are the major source of natural clear water resources. The Government Water and Sewage Authority is in charge of maintaining and improving the quality of natural and artificial water sources, of their rehabilitation and of preventing their pollution. The audit deals with **preventing and monitoring pollution and salination of water sources, and their recovery**. Found that past activities of defense industries and of IDF bases are the primary source of pollution in the coastal aquifer, which is a vital source of clear water supply to Israel's water resources. The Water Authority, the Ministry of Finance and the Ministry of Defense, which are the bodies responsible for treating pollution, particularly that derived of defense industries and IDF bases activities, have not yet completed performing rehabilitation activities to treat the pollution. The relevant bodies – the Water Authority, the Ministry of Defense, the Ministry of Finance, the Ministry of Environmental Protection and the Ministry of Agriculture and Village Development – should act to rectify the deficiencies detailed in this report and examine implementation of its recommendations, including formulation of a multi-year plan to treat pollutions, allocating financing resources according to determined priorities and act to remove pollutants from the various aquifers.

Our office also audited **the debt management at Israel Electricity Corporation Ltd.** Over recent years the IEC debt decreased: in December 2020 it decreased to NIS 30 billion, a reduction of 42.3% compared to 2012; and the IEC financial ratios have improved: in 2020, the debt ratio to EBITDA was 3.99 compared to a ratio of 8 in 2013. As a result, the capital raising conditions of the company improved, and the interest carried on the latest capital raising process was the lowest since the company began raising capital. The improvement in the financial situation of IEC over the recent years and the reduction of its debt by 2017 are an amendment to the deterioration in its financial situation derived from crises, and a return





to the situation prior to the fuel crisis and the global financial crisis of 2008 and 2009. In 2018 two agreements were signed between the IEC and the State – assets settlement and electricity market reform, which lead to an additional improvement in IEC's financial situation and to further reduction in the debt status. The audit showed that analysis of the factors that lead to reduction in the debt clarifies that this was made possible mainly due to one-time natured events and not as a result of ongoing steps taken by the company. 16% of the reduced debt is attributed to the actions taken to reduce the debt rate, and some of these actions were preformed, at the expense of investments in developing the electricity. It should be noted that the electricity sector is going through major changes that require the investments of significant resources. This places the continued improvement in the company's financial situation at risk. Adaptations to these changes will be required in order to prevent deterioration in the company's situation. The IEC and government bodies must provide the electricity requirements of the economy while maintaining the company's financial resilience.

The State Comptroller's office places special emphasis on following up the rectification of the deficiencies raised in its reports, and I intend to act to significantly strengthen and expand follow-up audits. This report includes four follow-up audits regarding these issues: **Public transportation – use of Rav-Kav cards and payment applications; Inter-city Roads Maintenance; Exercise of tax benefits by the Tax Authority; Foreign currency Balances Management by the Bank of Israel.** The follow-up audit on the subject of **Foreign Balances Management by the Bank of Israel** showed that over the past decade, following implementation of the Bank of Israel Law 2010, the activities of the Bank of Israel on the foreign currency market have been regularized. As part of the regulation process, there is a frequent examination of the need for change in the principles on which the appropriate level of long-term foreign currency reserves, and the guidelines for investment policy. In addition, most of the deficiencies raised in the previous report published in October 2012 have been rectified, including the lack of procedures to regulate the activities of the Bank of Israel and to handle risks in the reserves portfolio in general and in radical events in particular. At the same time, a significant increase over the past decade in the rate of foreign currency reserves held by the Bank of Israel, in addition to global financial developments, caused a deviation in February 2021 of USD 75 billion from the top echelon of the rate set by the governor. In addition, it increased the investment risks and created extensive liabilities in the bank balance to the scope of NIS 555 billion, most of which are related to accrued balances, and reduced bank capital to an accumulated capital deficit of approximately NIS 70 billion, as of December 2020. In order to return to the appropriate investment rate in the foreign currency reserves and to reduce the foreseen risk to the bank's reputation, a contingency plan should be prepared to examine the monetary committee, in order to utilize surplus reserves effectively in suitable circumstances.

It should be noted that one of the chapters prepared as part of this report dealing with cyber security, is going under confidentiality procedures and is not included in the report.





**This report was conducted by the Economic departments Division in the State Comptroller's Office. I wish to thank the employees of this division and the Office staff involved in writing the report for their professional, thorough, efficient, and challenging work, especially in the circumstances created by the Covid-19 pandemic.**

It is not unnoticed that audited bodies took positive actions. In accordance with the State Comptroller's Law, these actions have been properly reflected in this Report, in order to provide a whole picture of the situation indicated by the audit. The audited bodies are obligated to act quickly and efficiently to rectify the deficiencies raised in this report, in order to promote the public service in Israel, and thus to improve the quality of life and of the environment of the public.

**Matanyahu Englman**

State Comptroller  
and Ombudsman

Jerusalem, October 2021









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## Chapter 1

# Systemic Issues









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Systemic Issues

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## **National Programs for Developing the North of Israel**









## National Programs for Developing the North of Israel

### Background

The Northern District<sup>1</sup> featured disparities in most areas of life in comparison to other districts, including the areas of employment and wages, higher education and education, health and negative migration. Following is a description of the situation in the northern district as detailed in Government Decision 2262<sup>2</sup> (the data relates to the years 2013–2016): the average salary of employees in the northern district is the lowest compared to other districts. The rate of earners with salaries that do not exceed minimum wage, the unemployment rate, the poverty rate and the negative migration rate are the highest compared to all other districts, except the Jerusalem district. This data shows that the young population does not remain in the district. The northern district is characterized by the dominance of traditional and mixed traditional industries, suffering from low productivity. According to professionals in the Ministry of Tourism, the northern district has unrealized tourism potential. In the field of higher education and education there are also major differences in academic achievements, in the rate of matriculation graduates and in the number of graduates with 13 school years and over and in the number of higher education students compared to other districts. There are also disparities in the field of health: life expectancy in the northern district is two years lower than the national average, the number of doctors per 1,000 capita in the northern district is the lowest compared to other districts, the infants mortality rate is second highest after the south district and the number of beds per population size is the lowest, following the south district.

In January 2017 Government Decision 2262 regarding the "Economic development of the northern district and complementary steps for Haifa" (Government Decision 2262 or Decision 2262) was made, in which the government decided to activate a multi-year program for economic development of the northern district and to carry out complementary steps for Haifa.

The multi-year program was scheduled for years 2017–2021, where most of the program sections would be performed in 2017 and 2018. The program contains eight chapters: general, economic development, education and higher education, development of transportation

1 In the government decision "the Northern District" – as defined by the Ministry of the Interior.

2 Government decision 2262 "Economical development of the Northern District and complementary steps for the city of Haifa" (8.1.2016).





infrastructure and expanding transport accessibility, provision of social and public services, reinforcing local authorities, formulating strategic steps for economic development in the interim range and general development of Haifa. The program budget totaled NIS 19.3 billion of which NIS 17.3 billion were allocated to the northern district ranging from the Golan Heights and Upper Galilee in the north and to the Beit She'an Valley and Menashe Hills in the south.

### Key figures

**NIS 17.3  
billion**

The total budgets for the program allocated to the northern district by Government Decision for a multi-year program for years 2017–2021.

**46%**

The rate of northern residents who think that there has been no improvement in the field of employment over the past four years<sup>4</sup>.

**NIS 12  
billion**

The budget allocated for transportation and public transport infrastructure projects in the northern district for 2017–2021.

**59%**

The work force participation rate in the northern district in 2019 (58% in 2016) – the lowest of all districts, except for the Jerusalem district.

**NIS 2.8  
billion**

Total incremental budget for the program<sup>3</sup> according to the government decision.

**28.6**

The average number of persons requiring medical treatment per 1,000 capita in the northern district from 2013–2017. The highest rate of all districts.

**NIS 842  
million**

The budgets allocated for projects for general development of the northern district as part of the economic program.

**1.5**

The number of hospital beds per 1,000 capita in 2018. The lowest rate of all districts.

<sup>3</sup> Incremental – additional budget compared to previous years.

<sup>4</sup> From a public participation survey conducted for the State Comptroller's Office in February 2021.





## Audit actions



From August 2020 to February 2021 the State Comptroller's Office examined the decision-making process of Government Decision 2262, its effects and its implementation in the areas of economy, tourism, energy, education, health and transportation. The State Comptroller's Office also examined the implementation of the strategic steps determined in the Decision. The audit was carried out at the Galilee Development Authority in the Ministry of Economy and Industry (the Ministry of Economy), at the ministries of Finance, Tourism, Health, and Energy, at the Ministry of Transport and Road Safety (the Ministry of Transport), the Jewish National Fund and at Netivei Israel – National transport Infrastructure Company Ltd. Supplementary examinations were carried out at the Ministry of Defense.

In February 2021 two focus groups were conducted for the State Comptroller's Office on the subjects of tourism and health attended by senior managers, as well as a public participation survey<sup>5</sup> to learn about the standpoints and perceptions of northern district residents regarding the effectiveness of the State's investments in the district in terms of transportation, education, health, employment and personal security.

## Key findings



**Strategic work to formulate a multi-year program** – the role of a strategic work is to examine the existing disparities and the appropriate steps to reduce them, to suggest possible alternatives and to consider them in terms of cost effectiveness. The audit found that no comprehensive strategic work was done prior to the government decision on the subject. Moreover, the multi-year program was not based on various works by government ministries and other entities. It was also found that the work was prepared according to budgets that had already been approved to the government ministries and therefore included only some of the solutions proposed in the previous works. In the absence of any documents indicating and supporting the process of the strategic work, it is impossible to figure why some of the solution proposed in the professional work were not expressed in the multi-year program, and whether any alternatives were considered or if it was examined in terms of cost effectiveness.

<sup>5</sup> The survey conducted within the north communities was conducted through filling online questionnaires and telephone interviews. The sample included 1,033 northern district residents over age 18–526 from the Jewish society and 507 from the Arab society.





**👎 The rate of incremental budget of the total program budget** – it was found that of the NIS 17.3 billion budget for the multi-year program to develop the northern district, NIS 2.8 billion derived from incremental budgets. The remaining amounts originated from previous government decision, previous budget agreements and existing government ministries programs designated for the northern district. It was further found that over a billion NIS of the budget depends on fulfilling support tests and additional conditions, or it requires groundwork to exercise, and as such in order to exercise these budgets the relevant government ministries need to make changes in the directives and support tests.

**👎 Monitoring the effectiveness of the multi-year program and the contingency program** – Government Decision 2622 determined that the effectiveness of the programs receiving budgets as part of the decision will be examined, and the contingency program will be considered accordingly. The multi-year program did not set measurable goals that would enable examining the effect of the decision on various areas and no responsible entity was appointed to examine the effectiveness of the various programs. In fact, the effectiveness of many actions detailed in Government Decision 2262 was not examined<sup>6</sup>, nor was any contingency program formulated for the multi-year program.

**👎 Implementation of the Government Decision in the field of Health**

- **Incremental budget allocation** – the program allocated NIS 2.5 billion in the area of health for 2017–2020. Of this budget, 62.6% (NIS 1.5 billion) are allocated for the continuation of existing programs in the Ministry of Health base budget, and 37.4% (NIS 930 million) are an incremental budget as defined by the Ministry of Finance as part of a multi-year investment.
- **Health situation in the northern district compared to other districts** – data provided by the Ministry of Health and the Central Bureau of Statistics for 2016–2019 show that the life expectancy in the northern district (81.8 years) is lower than the other districts (except for the south district) and the rate of infant mortality per 1,000 capita in the northern district (2.6 infants per 1,000 capita) is among the highest in Israel. This data, together with the rate of professional personnel in the medical field, which is of the lowers in Israel, such as the rate of doctors per capita in the northern district, which is 2.2 doctors per 1,000 capita for 2017–2019, and which is less than 40% of the rate of doctors in the Tel Aviv district and 50% of the rate of doctors in the Haifa, Central Israel and Jerusalem districts, indicates that there is need to handle the situation in the fields of medicine and health in the northern district and improve it.

<sup>6</sup> Except for evaluating the effectiveness of subsidizing development costs for land development in industrial areas lead by the Strategy and Policy Planning Department at the Ministry of Economy and Industry.





- **Constructing infrastructures** – Decision 2622 determined allocating a total of NIS 235 million for 2017–2020 during the life span of the multi-year program for constructing infrastructures or general, psychiatric and geriatric wards in the northern district and opening beds in required areas at the Ziv, Nahariya, Ha'emek and Poriya hospitals. The Ministry of Health allocated NIS 76.9 million for general hospitalization beds and NIS 72 million for geriatric beds. However, the differences between the northern district and other districts concerning hospitalization beds were not reduced. It was found that during 2015–2017 the areas where the rate of visits to the ER (average of 272–345 per 1,000 capita and an average of 111–115 per 1,000 capita) is the highest in the north, whereas in 2019 the rate of general hospitalization beds per 1,000 capita in the north is 1.5, which is the lowest in Israel. Despite Government Decision 2262 the bed rate in the north decreased.
- **Shortening waiting times for medical treatment** – Decision 2262 determined that as part of the national program to shorten waiting times NIS 520 million would be allocated for the benefit of shortening waiting times and increasing the number of surgical operations in the public health system in the northern district. As of the second quarter 2019 the northern district residents have to wait longer than Tel Aviv district residents for orthopedic treatments, gynecology, ophthalmology and dermatology – the waiting times ranges between 28.5 days to 38.6 days. As a result and as shown in the public participation, northern district residents are subject to prolonged waiting for receiving these services, or are obliged to travel to the central district to receive them.
- **Mental health** – as of 2018, the northern district, as well as the south district have the lowest rate of beds in the area of mental health compared to all other districts (0.28 per 1,000 capita). The audit found that regarding the Mazor Mental Health Center, which is the only one in the north, the hospital rooms are densely populated and that no plans have been prepared to relocate the mental health hospital and the alternative location has not yet been decided, despite that fact that due to the land designation, an alternative location must be found by 2026. Moreover, during 2017–2020 NIS 24.8 million – 10.6% of the budget allocated for constructing infrastructures at the Mazor Health Center was utilized.
- **Capitation** – the capitation mechanism<sup>7</sup> did not determine that the budget allocated to the HMOs for geographical remoteness would be used to develop their services in the periphery. Government Decision 2262 determined that the Ministries of Finance and health should examine expanding periphery preference as part of establishing a new capitation formula. Until the audit completion date no new

<sup>7</sup> Capitation is the name given to the formula used to determine the allocation of sources to the HMOs by virtue of the National Health Insurance Law.





capitation formula was established and no corrections or changes were made to the existing formula.

- **Public participation** – in regard to waiting times for appointments and availability of medical services in the northern district it appears that 33% of residents do not think there has been any improvements over recent years, and over 40% think that the change is mediocre. Moreover, 40% of responders stated they were referred to medical centers outside of the northern district, mostly to a medical center in Haifa.



#### **Implementation of the government decision in the field of education**

- **Matriculation entitlement data** – it was found that as of December 2019, although investments to the extent of NIS 859 million out of the NIS 945 million were utilized, this has not yet reduced the disparities in matriculation entitlement data between the northern district and all other districts. In 2019 the rate of the northern district matriculation entitlement totaled 76.1%, a lesser rate to the matriculation entitlement rate of the central district (86.1%), Haifa district (82.1%), Tel Aviv district (82%) and south district (77.8%) and higher only than the Jerusalem district (72.4%).
- **Education in the subjects of mathematics, sciences and English** – in the scientific subjects and in English the rate of pupils taking the matriculation exams at five learning unit levels (the highest level) in the northern district was in last place relative to the general rate in Israel. Moreover, there are significant disparities between the northern district and other districts, for example, in 2019 the rate of those who took the matriculation exam in five unit level computer sciences in the northern district was 5.3% compared to 13.1% in the central district.
- **Establishing a university in the north** – over 15 years have lapsed since Government Decision 3578 of 2015 was taken, the Ministry of Education, Culture and Sport and the Ministry of Water and Higher Education have not reported any progress on the matter, and the process for establishing a university in the Galilee has not been promoted.
- **Public participation** – over 40% of survey respondents think that in their settlement of residence there has been no improvement in the number of classes for studying sciences, in the number of new classes for other learning subjects, in the organized transportation to schools and extra curricular activities and in the diversity of these activities.



#### **Implementation of the government decision in the fields of economic development and infrastructures.**

- **Attracting the hi-tech industry** – Government Decision 2262 determined that the Ministry of Economy should act, among others, in the following areas in the northern district: attracting hi-tech industries and creating employment





opportunities, increasing productivity, promoting competitive and advanced industries, attracting investments and entrepreneurs, reinforcing small and medium size businesses and developing industrial areas. Following Government Decision 2262 the Ministry of Economy CEO directive 4.18 was changed<sup>8</sup>. The Decision stated that the change and budget in favor of Ministry of Economy CEO directive 4.18 were designated to encourage the move of hi-tech industry companies to the northern district. Despite the preference given by the directive to the northern district, the Ministry of Economy data shows that in 2017–2018 eight companies received assistance, 74% of the total NIS 90 million budget determined by the Government Decision were utilized, but in fact no companies moved to the northern district following the directive changes; it was found that the changes in the CEO directive 4.18 did not contribute to the transfer of companies to the northern district, including hi-tech companies.

- **Creating additional employment opportunities** – following Government Decision 2262 the Ministry of Economy CEO directive 4.17<sup>9</sup> was changed so that in 2017–2018 an additional course of assistance was added (Course E) – “Assistance for hiring additional employees in the peripheral municipalities 1–4 of the northern district”, the course was designed to create quality places of employment characterized with high salaries. The audit found that in 2017–2018 two companies received assistance from the designated course for the northern district, and 20 additional employment places were added to the northern district because of this course (compared to 33 companies from the north that received assistance from the other courses published during these years). Therefore, the designated course did not achieve the objective of creating quality high paid employment opportunities.
- **Assistance to businesses in the north** – the audit found that during 2017–2018 the assistance to businesses in the northern district decreased according to the Ministry of Economy CEO directive 4.17 (from NIS 50 million in 2016 to NIS 9 million in 2018) and less applications were submitted compared to 2014–2016; this decreasing trend continued in 2019 where assistance totaled NIS 6 million. Therefore, the changes did not lead to increase the demand for assistance.
- **The assistance program for small and medium sized businesses** – in January 2017 the Ministry of Economy began formulating a program to increase productivity of small and medium sized businesses while integrating an evaluation and measurement mechanism (by random allocation to some of the applicants). The audit found that even though the Government Decision 2262 was published on 8.1.17 the program for small and medium sized businesses was published on

8 Ministry of Economy CEO directive 4.18 – “High salary program”.

9 Ministry of Economy CEO directive 4.17 – “Assistance aid program for recruiting additional employees for business in Israel”.





21.12.17, and the random allocation mechanism set in this program reduced the extent of the program's budget realization. The budget utilized for the program totaled NIS 10 million out of the NIS 30 million allocated, and the random allocation data was not used for any research.

- **Attracting investments and entrepreneurs to the northern district –** Decision 2262 determined that the Foreign Investments and Industrial Cooperation Authority at the Ministry of Economy (Rashpat) would act to market the northern district as an attractive target for investments, while locating the obstructions and providing recommendations for their removal. It was found that the Rashpat acts to attract investors to Israel with a broad overview and does not perform any designated marketing for the northern district.
- **The economic data of the northern district compared to the rest of Israel** – as of 2019 the northern district remains low on the economic indexes compared to other districts and for most indexes the improvement that occurred is similar to the average improvement in Israel. For example, in 2018 the income per capita for the northern district totaled NIS 5,744 compared to the national average of NIS 7,801 and the rate of change compared to 2016 was 10% in the northern district compared to the 11% national average. Therefore, the northern district development program and the allocation of designated budgets for a variety of economic areas according to Government Decision 2262 did not sufficiently contribute to any higher improvement in the north compared to the national average in all indexes.
- **Public participation** – 13% of respondents work outside the northern district. 69% of respondents earn less than the average salary, and 60% estimated that their salary is lower compared to the salary for similar jobs in other districts.



#### **Implementation of the government decision in the field of tourism**

**Allocating budgets for developing public infrastructures** – the budget for developing public infrastructures in the northern district set in the government decision, for the sum of NIS 50 million, was determined according to the Ministry of Tourism estimates based on budget utilization in previous years and did not reflect any preference of the northern district. The multi-year program did not reflect any preference for the northern district in 2017 and 2018 and the budget was lower than the actual assistance transferred for each of the years 2015 and 2016 (NIS 57 million and NIS 65 million, accordingly). In addition, the audit found that in 2017 and 2018 the total assistance for developing public tourism infrastructures in the north (NIS 56 and 20 million) and the assistance rates relative to the entire country (26% and 8%) are low and that in 2019 to which the Government Decision 2262 did not refer the assistance and its rate to the northern district increased compared to other districts. The audit





found that Government Decision 2622 for 2017 and 2018 did not increase the assistance to the northern district.

- **The policy of the Ministry of Tourism to develop infrastructures in the north** – the Ministry of Tourism procedure for the Development of Public Tourism Infrastructures (Appendix A to the procedure) does not include any reference for promoting tourism in the northern district in 2017–2018 and the audit found that the Ministry of Tourism policy for 2017–2018 was directed at promoting tourism in the south district and did not include promoting the northern district.
- **Public participation** – a meeting held as part of the public participation, with position holders from the private and public sectors in the northern district, presented the following major obstructions – absence of tourism leadership in the northern district, absence of any proper handling of tourism infrastructures, no growth in accommodations in central towns and inadequate supervision of tourism assets.



#### **Implementation of the government decision in the field of energy –**

- **Support of remote natural gas consumers** – in the calls for proposals published by the Ministry of Energy during 2017 and 2018 no preference was given to the northern district and no applications were submitted for connecting remote consumers in the Haifa and northern districts. Therefore, the NIS 35 million allocated in Government Decision 2262 for supporting remote gas users in the northern district were not utilized.
- **Establishing natural gas fueling stations** – in March 2018 the Ministry of Energy issued a call for proposals (51/2016) for the submission of proposals for a program that combines grants and a safety net for the establishment of compressed natural gas fueling stations; the call for proposals did not assign any preference to fueling stations in the northern district. Moreover, out of the 37 stations that were awarded grants by virtue of the call for proposals issued by the Ministry of Energy on March 2018 for establishing compressed natural gas fueling station, only one station in the Haifa district complied with the requirements and as of concluding this audit all other winners, including 5 stations in the Haifa and northern districts did not comply with requirements and therefore the agreements therewith are expected to be cancelled and the establishment of natural gas fueling stations will not be promoted.
- **Layout of a distribution network and connecting consumers** – a significant portion of the natural gas distribution outline north of the Tiberias – Safed – Kiriat Motzkin aerial line was not in fact established, despite the fact that the original schedules for its establishment were for 2015–2019. Moreover, the rate of connected consumers actually using natural gas in the north (10 out of a potential 168) is the lowest of all distribution regions (except for the Jerusalem district where





there was no consumption), as well as the accrued consumption as of 2020 in the north (36.6 million MC).

- **Budget allocation in favor of upgrading the natural gas distribution network** – as part of the calls for proposals a total budget of NIS 283 million was provided for all districts and milestones have been set to execute, where NIS 99 million were allocated in favor of upgrading the distribution network in the north (Haifa and the Galilee) – as of the audit completion date, NIS 42 million of the NIS 99 million attributed to the north were paid, according to the milestones set in the calls for proposals.



#### **Implementation of the government decision in the field of transportation –**

- **Developing transport infrastructures and increasing transportation accessibility** – developing transport infrastructures in the northern district is a subject with the highest budgetary extent – NIS 12 billion as set in Government Decision 2262. However, these projects were in various planning stages even before the government decision was made, and were even mentioned in the Ministry of Transport work plans and in the Netivei Israel five year plans, and partially in the State budget for 2017–2018. Moreover, the project for developing Metronit lines in the Haifa metropole, one extension out of the planned 6 extensions belongs to the northern district and the audit indicated that there are delays in completing 6 out of the 11 transportation projects.
- **Public participation** – the public participation process showed that residents have noticed great improvements in roads and transport infrastructures and in public transportation, yet at the same time most residents do not feel any significant improvement in arrival times to work, to major highways or to medical centers.



**Strategic steps for developing the northern district** – Government Decision 2262 determined the following steps as strategic steps for economic development in the northern district: examining relocating IDF bases to the northern district; examining relocating government companies with technological activities and extensive employment capacities to the northern district; formulating a multi-year program to expand existing industrial areas and establish new areas in the northern district; examining establishment of a complementary airport to Ben Gurion Airport in the northern district and recognizing NIS 400 million worth projects as “national projects”. The government decision did not include operative steps or budget allocations<sup>10</sup> or determined schedules for execution. By the audit completion date, an examination of the option to relocate IDF bases to the northern district had not been completed, no actions were taken into examine relocating government companies with technological activities and large employment capacities to the northern district, no final decision had

<sup>10</sup> Except for the budget for projects recognized as “national projects” by the JNF.





been made on the location of a complementary airport to the Ben Gurion Airport and projects recognized as “national projects” had hardly been promoted. For example, as of the audit completion date, only NIS 37.5 million of the NIS 400 million allocated by government decision for projects recognized as “national projects” had been used. These strategic steps could have been the generators of change and the growth engines required to significantly improve the situation in the northern district, and lead to improvement in all areas of life, but these steps were not sufficiently promoted.



**The program to increase work productivity** – the Ministry of Economy formulated a program to increase productivity, within during 2017 and 2018 39 assistance application in the northern district were approved for which grants totaling NIS 60 million were given.

**Developing transport infrastructures** – developing transportation infrastructures and increasing transportation accessibility in the northern district had the highest budget allocation in Government Decision 2262, for the total of NIS 12 billion.

## Key recommendations

- 💡 It is recommended that the Periphery, Negev and Galilee Development Ministry and the Ministry of Finance prepare goals and indexes for all of the actions derives from the program, and examine, with the assistance of all the relevant ministries, the need for formulating a contingency program and operate accordingly. It is further recommended that when submitting for government approval a multi-year program for the development of a region, and particularly the north, the decision should include measureable goals so that program effectiveness can be evaluated. The program should include appointing a responsible entity to evaluate the effectiveness and provide a reporting system to the steering committee and the government.
- 💡 It is recommended that the Periphery, Negev and Galilee Development Ministry, the Ministry of Economy and the Ministry of Finance when preparing a multi-year program for the development of a region, and particularly the north, conduct a designated strategic work that includes a comprehensive view of the disparities, obstructions and solutions, while examining previous professional works formulated by the various ministries, cost analysis – compared to the effectiveness of the various alternatives and promotion of a holistic solution that will enable contending with all issues requiring remedy.
- 💡 It is recommended that the Ministry of Health operate to improve and expand the medical services provided to residents of the north, examine the population requirements and the existing obstructions for residents, at medical centers and hospitals, that prevent receiving or providing proper and optimal medical care. Treatments availability and





accessibility should be provided, existing infrastructures improved and skilled and appropriate medical staff recruited. The Ministry of Health should verify that the budgets transferred to benefit medical services bring about the required change and it is recommended that the Health and Finance Ministries examine changing the capitation formula to improve medical services in the periphery.



It is recommended that the Ministry of Education review the existing education disparities in the northern district, and particularly the entitlement to five unit level matriculation in the subjects of mathematics, English and sciences, and devise a plan for their reduction. It is further recommended that the Ministers in charge of higher education and of Periphery, Negev and Galilee development complete their review of establishing a university in the Galilee, and report to the government on the subject, as determined by Government Decision 3578.



It is recommended that the Ministry of Tourism complete the preparation of the regional programs and assistance plans that will express the government policy of the reinforcing the north and take into consideration the obstructions indicated in the public participation process. It is also recommended that the Ministry of Tourism establish criteria for assistance adapted to relevant tourism events in the northern district in terms of size and extent.



It is recommended that the Gas Authority continue to examine the obstruction preventing development of gas infrastructures in the northern district and connection of north residents to the distribution network, and find the means for their removal in order to encourage consumers from the northern district to connect to the natural gas network and consume natural gas as part of economic efficiency, and to thereby reduce gaps between the northern district and all other districts.



The State Comptroller's Office recommends that the Ministry of Transport act to complete the six projects included in Government Decision 2262 with budgeting.



In order to reinforce the northern district, which was characterized for many years by a low socio-economic level, negative migration and disparities in most fields of life compared to all other districts, including employment and salaries, education and health, genuine transformation is necessary through generators of change and growth engines. The relevant government ministries should act to promote the strategic steps included in Decision 2262 in order to advance growth engines in the north, including:

- The Ministries of Finance and Defense and the Israel Land Authority should complete the strategic work regarding the relocation of IDF bases to the northern district according to the government decision and formulate recommendations to promote the issue.
- It is recommended that the Ministry of Transport and the Planning Administration act, each under their vested authority, together with relevant entities, to complete the strategic work required and act to promote a final decision regarding the

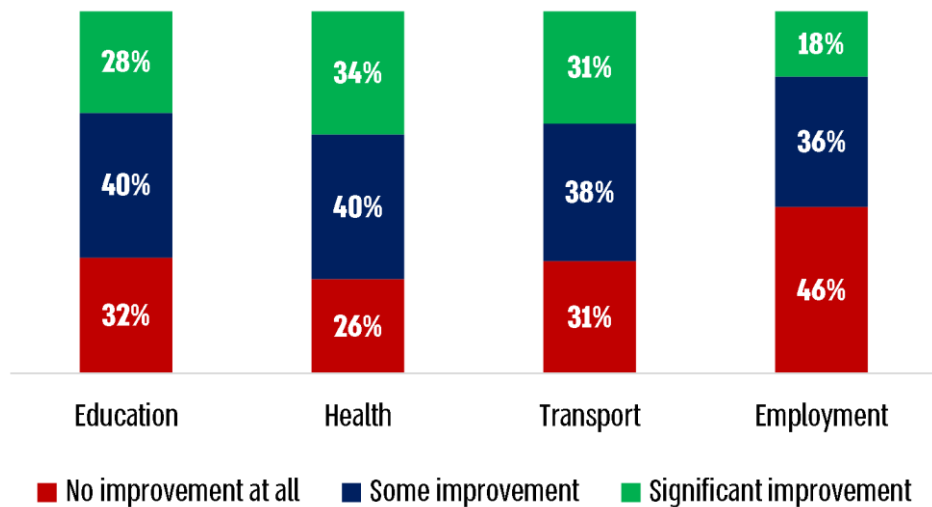




location of the supplementary airport to Ben Gurion as well as the planning process, while relating to issues of safety, security and economy as raised by the professional entities, taking into consideration the effect of the decision on the north and south, and operate accordingly to establish a supplementary airport to Ben Gurion.

- The Budgets Commissioner at the Ministry of Finance and the Head of the Government Companies Authority or their representatives should establish a joint team to examine relocating the activities of government companies of technological nature and with large employment capacity to the northern district, as determined by Government Decision 2262.

### The perception of the improvements done in the four years until February 2021 by the residents in the northern district



According to the public participation survey.

## Summary

In 2016 the government decided on the formulation of a strategic multi-year program to develop the northern district. In 2017 the multi-year program for developing the north was





presented. The program included many government ministries that handle a variety of areas, significant government investment and change generating steps.

An examination of the implementation of the program by government ministries in the various areas indicated that the programs did not generate an actual change in the relevant fields of life, whereas for some projects included in the government decision, the obstructions impeding various areas in the northern district were not examined, and therefore the preference given to the northern district was not effective. Some of the budgets were not used and objectives determined in the decision were not achieved.

It was also found that the strategic steps for financial development in the interim range in the northern district, which may have become the necessary generators of change and growth engines to substantially improve the situation in the northern district and as a result lead to improvement in all areas of life, were not sufficiently promoted.

An examination of current poverty levels and disparities between the northern and other districts in various areas, including employment and salaries, education, higher education and health, indicated that since the government decision was taken there was no fundamental improvement in these disparities, and the metrics of the northern district are lower compared to all other districts on most of the examined indexes.

The State Comptroller's Office recommends that the government ministries conduct a review of the situation of the northern district in comparison to other districts and the effectiveness of the actions included in the government decision in order to study their effect and promote a contingency program to the program determined by Decision 2262 so that disparities between the northern district and all other districts are reduced.





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Systemic Issues

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# **Investments Management at Various Entities**









## Investments Management at Various Entities

### Background

The management of investments of various entities in the public sector (institutional entities, government companies, statutory corporations and local authorities) may have an impact on their financial stability and ongoing activities. These entities are required to implement a comprehensive investments policy that will address the entity's methods of investment in a suitable way for its activities, its exposure to risks and its business strategy, alongside managing the risk of liquidity according to cash flow forecasts. The investments funds serve the entities for different time ranges, and are invested according to the entity requirements or for the funds designated objectives.





### Key figures

**NIS 9.4  
billions**

The value of current investments on 30.6.20 of institutional bodies, government companies and statutory corporations (government entities) audited.

**NIS 6.4  
billions**

The value of investments designated for pensions on 30.6.20 of the government entities audited.

**3.83%**

The average annual yield for 2017–2019 of current investments of the audited institutional bodies.

**3.25%**

The average annual yield between years 2017–2019 of current investments of the audited government companies and statutory corporations.

**3.91%**

The average annual yield between years 2017–2019 of pension investments at the audited government companies and statutory corporations.

**46%**

Authorities hold long-term investments portfolios<sup>1</sup> (31.12.19).

**NIS 4.9  
billions**

The value of the long-term investments of the audited local authorities (30.6.20).

**2.4%**

The average yield for years 2017–2019 of long-term investments of the audited local authorities.

## Audit actions



From June to December 2020 the State Comptroller's Office audited aspects of the financial investments management in several institutional bodies, government companies, statutory corporations and local authorities with significant investment extents. The investments can be current self-made (nostro) or investments designed to cover pension liabilities. The audit was conducted at the following bodies: Kanat – The Insurance Fund for Natural Risks in Agriculture Ltd; Karnit – The Road Accident Victims Compensation fund; Ashra – The Israel Foreign Trade Risks Insurance Corporation Ltd; The Israel Electric Company Ltd; The Haifa Port Company Ltd; The Ashdod Port Company Ltd; The Israel Airports Authority; The Quarries Rehabilitation Fund. The audit was also conducted at the Ministry of the Interior and at 50 local authorities through a

<sup>1</sup> The investments portfolios include tradable securities (long-term investments portfolio).





questionnaire. Supplementary audits were conducted at the Government Companies Authority and at the capital market Insurance and Savings Authority; At the Federation of Local authorities and at the Local Government Economic Services Ltd. (Mashcal).

## Key findings



### Institutional bodies – Kanat, Karnit and Ashra



**The composition of the institutional bodies investments portfolios** – there are differences in the portfolio composition of the various bodies audited – Kanat, Karnit, Ashra. The government institutional bodies invest 69%–79% of their assets in bonds and do not invest in an alternative channel of investment funds.



**The yields of investments portfolios** – there are differences in the institutional bodies yields for the period from 2017 to June 2020, and between them and the advanced study funds and additional tradable indexes. These differences derive from the diversity in the portfolio components and their variant risk profiles as expressed, among others, in the exposure percentage to various assets and the different investment horizon needed for flow purposes of each body. Following is the data regarding the yields of the various bodies:

The body	2017	2018	2019	1–6.20
<b>Audited bodies</b>				
<b>Kanat</b>	4.22%	-1.06%	7.78%	-4.31%
<b>Karnit</b>	1.28%	2.47%	5.58%	-1.62%
<b>Ashra</b>	5.01%	-1.17%	10.36%	2.08%
<b>Comparative indexes</b>				
<b>Advanced study funds</b>	6.90%	-1.22%	11.94%	-5.10%
<b>TA 125</b>	6.87%	-2.44%	21.20%	-18.18%
<b>Tel Bond 60</b>	5.79%	-0.79%	7.37%	-5.49%

The source: the data of the audited bodies, data from net provident systems and data from the stock exchange processed by the State Comptroller's Office.



**ESG investments<sup>2</sup>** – the institutional audited bodies did not include ESG rules in their investments policies. Moreover, whereas they are not defined as institutional investors, the draft circular written by the Capital Market Authority on the subject is not expected to apply on them.

<sup>2</sup> Environmental, Social and Governance.





**Administrative issues in the work of the investments committee** – the investments committees of both Kanat and Karnit convened properly once a month, whereas from June 2018 to June 2020 the Ashra committee convened only seven times, but not each quarter; in all the audited bodies, despite having the required quorum<sup>3</sup> directors were absent from a significant portion of the investments committees<sup>4</sup>; a review of the various bodies protocols indicates that the Ashra protocols content is lacking, whereas at the Kanat and Karnit companies the protocols properly reflect the discussions held by the investments committees and enable comprehension of the considerations that formed the basis for the committee decisions. It was further found that the members of the Ashra company investments committee who are company employees are not signed on any declaration to prevent conflict of interests concerning their activities on the investments committee.

**Professional issues in the work of investments committees** – in 2000, in the absence of a quorum, the board of directors of the Ashra Company, did not approve the investments policy; Ashra does not compare the performance of the various portfolio managers in reference to yield related to various risk indexes ; it was only in March 2018 that a risks manager was appointed for Karnit; in the audited period no internal audits were conducted on the subject of investments at the Ashra company.

**Government companies and statutory corporations – the Israel Electric Company, Haifa Port, Ashdod Port, the Airports Authority and the Quarries Rehabilitation Fund.**

**Composition of investments portfolios** – there are differences in the portfolio compositions of the audited bodies in both current and pension investments portfolios. However, it should be stated that the investment percentage of audited bodies in government and concern bonds ranges from 69%–98% and they do not invest in alternative channels, such as investment funds.

**The yield of current investments portfolios** – there are differences in the yields of government companies and statutory corporations for the period from 2017 to June 2020, and between the advance study funds and other selected indexes. These differences derive from the diversity in the portfolio components and their variant risk profiles as expressed, among others, in the exposure percentage to various assets and the different investment horizon required for flow purposes of each body. Following are the yields data of the various bodies:

<sup>3</sup> Legal quorum.

<sup>4</sup> In 44% of the Kanat meetings one member was absent; in 32% of the Karnit meetings one member was absent; In Ashra – only five out of sixteen meetings there were two directors present.







The body	2017	2018	2019	1-6.20
<b>Audited bodies</b>				
<b>Haifa Port</b>	4.82%	-1.85%	9.30%	-4.71%
<b>Ashdod Port</b>	3.27%	-0.62%	5.60%	-1.36%
<b>Airports Authority</b>	3.60%	-0.93%	6.60%	-0.60%
<b>Quarries Rehabilitation Fund</b>	3.35%	-0.43%	6.23%	-1.65%
<b>Comparative indexes</b>				
<b>Advanced study funds</b>	6.90%	-1.22%	11.94%	-5.10%
<b>TA 125</b>	6.87%	-2.44%	21.20%	-18.18%
<b>Tel Bond 60</b>	5.79%	-0.79%	7.37%	-5.49%

The source: the audited bodies data, data from net provident systems and data from the stock exchange processed by the State Comptroller's Office.

Moreover, the Airports Authority and the Quarries Rehabilitation Fund do not publish data regarding the current yields of their investments portfolios.

 **Administrative issues in the investment committee's work** – the investments committee of the Airports Authority convenes at least twice each quarter and the investments committee of the Haifa Port convene sometimes each month and sometimes only once in several months; at the Haifa Port and the Quarries Rehabilitation Fund there was no required quorum at the investment committee meetings for some of the period from January 2017 until June 2020; a review of these bodies protocols indicates that, except for the Airports Authority, the content of the protocols of the remaining bodies does not properly reflect the discussions and does not enable understanding of the considerations that formed the basis for the committee decisions. It was also found that as of the audit completion date, the investments committee members at the Haifa Port and the Airports Authority did not sign declarations to prevent conflict of interests, and that at the Haifa Port, the Ashdod Port and the Israel Electric Company the matter is not regulated by a procedure.

 **Professional issues in the work of the investment committee** – the Quarries Rehabilitation Fund management did not approve the investment policy in 2017 and the Electric Company board of directors does not approve the investment policy of the investment for pension portfolio; the Electric Company, contrary to all other audited <sup>5</sup> bodies, does not use the services of a financial advisor, despite it being possible by




<sup>5</sup> The investments portfolio of funds in trust designated for coverage of actuary liabilities for pension payments to employees for salary components that are not pensioned and liabilities related to termination of employer-employee relations.





internal procedure and despite the major investment amounts in its investments for pension portfolio. The Electric Company, Airports Authority and Quarries Rehabilitation Fund do not use various risks indexes to compare the performances of their portfolio managers; the Electric Company and the Quarries Rehabilitation Fund did not conduct a risks analysis of their investments portfolio in the audited period; the Haifa Port, Electric Company and Airports Authority did not conduct any internal audit on the subject of investments in the audited period.


### Local Authorities


-  **The Monitoring of the Ministry of Interior over the Local Authorities investments management** – the Ministry of Interior does not have information concerning local authorities that manage an active portfolio and local authorities that do not manage active investment portfolios. Moreover, it was found that the Ministry of Interior does not monitor the existence of active investment portfolios in the various local authorities. Moreover, the monetary data that is reported by the local authorities to the Ministry of Interior and the public financial statements do not reflect the activity of the local authorities investments portfolios, and it is impossible to identify the extent of the investment portfolio, the yield gained from it and the portfolio investment channels.
-  **Distribution of the Investment portfolio holdings divided by the authority cluster** – there is a significant difference between local authorities with high socio-economic ranking and local authorities with low socio-economic ranking. For example, 82% of high ranking local authorities hold an active investment portfolio, whereas only 28% of low ranking local authorities hold an active investment portfolio. Furthermore the average long-term investments portfolio of top decile municipalities (not including Tel Aviv-Jaffa) totaled NIS 113 million, compared to NIS 30 million in low decile municipalities.
-  **The long-term investments portfolio yield** – the average accrued yield of local authorities for 2017–2019 totaled 2.4% and was low compared to the yields of advance study funds and the central compensation funds, which totaled 5% – 6% in the said period. The said differences derive from the diversity of portfolios compositions and different risk profiles.






The body	2017	2018	2019	1–6.20
<b>Audited bodies</b>				
<b>Local Authorities audited - with long terms investments for the years 2017–2019 (average yield)</b>	3.4%	-1.3%	5.2%	-1.6%
<b>Comparative indexes</b>				
<b>Advanced study funds</b>	6.9%	-1.2%	11.9%	-5.1%
<b>Principle compensation funds</b>	6.4%	-1.3%	10.9%	-5.0%

 **Administrative issues in the work of the investments committee** – 34% of the audited local authorities (17 out of 50) did not have an active investments committee as of 31.12.2019. Moreover, between years 2017–2019, 22% to 33% of local authorities with long-term investments portfolios did not hold meetings of the investments committee at the required frequency.

 **Ministry of Interior directives** – despite the professional advantages the Ministry of Interior did not set any directives regarding the obligation of the local authorities to create marker portfolios and/or contract professional financial advisors to determine policy, manage and review the performance of their investments portfolios. Moreover, the Ministry did not define any directives for the necessary supervision and control of budgetary pension funds of the local authorities employees.

 **Monitoring the investments committee activities** – in 2017–2019 78% of the audited local authorities that had active investment portfolios (14 out of 18 local authorities) did not hold discussions at management level on the investment committee activities<sup>6</sup>, although until the publication of circular 02/2020 the local authorities were not obliged to hold such annual discussions. Moreover, despite the risk and the significant extent of the local authorities investments portfolios, only at 4 out of the 50 local authorities that answered the questionnaire, the internal auditor conducted an audit of the investments committee activities. In addition, the Ministry of Interior did not conduct any initiated audit on the local authorities investments committees to fully and extensively examine the local authorities adherence to its directives. The Ministry did not

<sup>6</sup> Of 18 local authorities with active investment portfolios during 2017–2019, two local authorities held annual discussions and two held discussions in some of the years.





review the monitoring and control of the local authorities investments committees over the pension funds.



**Approval of the investment policy** – in most audited government entities the investment policy is approved annually.

**Procedure regulating the investment committee activity** – in most of the audited government entities there is a procedure regulating the activities of the investments committee. In addition, the Ministry of Interior published and updated directives to local authorities on this matter as part of the CEO circulars<sup>7</sup>.





**Using a marker portfolio to compare investments portfolio performances** – most audited government entities and some local authorities use marker portfolios to compare performances of investment portfolios.

**Conducting internal audits to minimize risks** – the Kanat company internal auditor prepared an internal audit report on the subject of reviewing investment houses internal audit reports in order to minimize the Company's exposure to risks of investment houses.

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## Key recommendations

### Public Institutional Bodies – Kanat, Karnit and Ashra




-  In order to examine the portfolio managers performances, it is appropriate to define a relevant comparative attributing index and use a variety of comparative attributing indexes, to maximize yields of investments portfolios.
-  It is recommended that Karnit, Kanat and Ashra continue to periodically examine their investment policies, the yields and investment diversity including a comparison to parallel institutional investors and customary indexes in the market, in order to achieve optimal yields from their investments portfolios.
-  It is recommended that all public bodies audited as part of this audit examine including ESG rules in their investment policy.
-  The Minister of Economy and Industry and the Minister in charge of The Companies Authority, should act to complete the appointment of directors in Ashra as required by law.

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<sup>7</sup> Rules for investing temporary surpluses accrued in the development funds and other temporary surpluses, memos: 08/94, 04/2008 and 02/2020.



**Government companies and statutory corporations – the Israel Electric Company, Haifa Port, Ashdod Port, the Airports Authority and the Quarries Rehabilitation Fund.**

-  In order to increase transparency of managing the funds of government companies for the public eye, it is recommended that the Government Companies Authority consider instructing government companies to regularly publish their investments portfolio yields in order to reflect the investment policy and the company considerations.
-  It is recommended that the Airports Authority and Quarries Rehabilitation Fund consider publishing the yields of their investments portfolios regularly.
-  In view of the large investment funds being managed, some of which are managed through investment managers, it is recommended that the Haifa Port, the Electric Company and the Airports Authority conduct internal audits on investments.

**local Authorities**

-  The local authorities that have an active investment portfolio should act to hold the discussions of investments committees as required and issue letters of appointment for investment committee members. It is also recommended that the Ministry of Interior, the local authorities and the Federation of Local authorities establish periodical training for the local authorities investment committee members to ensure they have the required and updated professional knowledge to execute their roles as members of the investments committee.
-  The Ministry of Interior should update its directives to include designated and detailed directives on supervision of investments committees, on management of local authorities employees' pension funds, including investment policies, methods for selecting provident funds and the tools to supervise and control its performance.
-  It is recommended that the Ministry of Interior examine the use of tools and relevant reference indexes, and the contribution and services of the financial advisors to the investments committee, particularly on all matters pertaining to local authorities that manage large portfolios, and adjust its directives accordingly. In addition, it is recommended that the Federation of Local authorities and the Local Government Economy Company Ltd assist the local authorities in improving their investments activity and in creating advantages to size in managing the investments portfolios, such as establishing a database of portfolio managers, professional external investments advisors and in professional training for the investments committee members.
-  It is recommended that the Ministry of Interior Audit Department include in its audits of local authorities an examination of attributing yields from investment portfolios and ensure the fulfillment of the directive. Moreover, all local authorities holding long-term investments portfolios with finances designated for development funds including Tel Aviv-Yafo, Holon, Rishon Lezion, Kfar Sava, Elad, Shafir, Carmel Coast, Sderot, Ofakim,



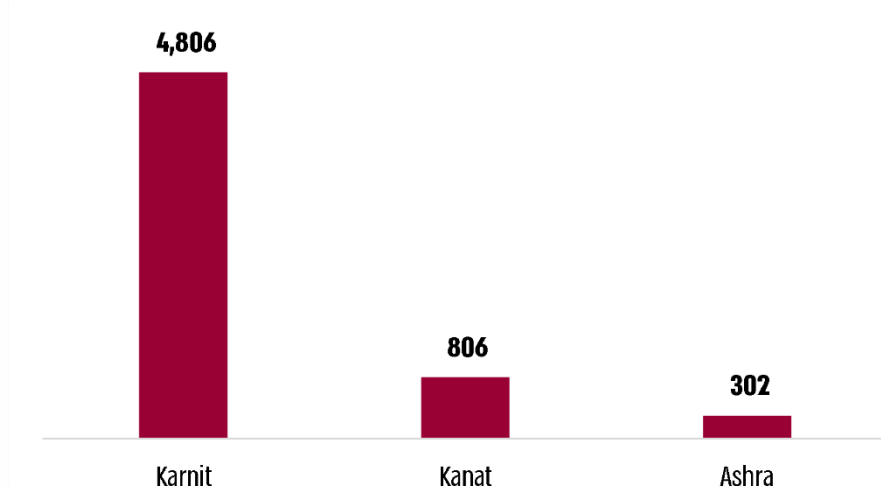


Bat Yam, Arad, Tirat Hacarmel, Tel Mond, Segev Shalom, Hadera, Haifa, and Mateh Asher should act to attribute yields in favor of the development funds.



In view of the large portfolio managed by a number of external portfolio managers in the audited local authorities, it would be appropriate that the Ministry of Interior and the auditors of the relevant local authorities conduct periodical audits to improve the authorities upholding of the Ministry directives and to examine and improve performances, in order to increase the local authorities benefit from the investment portfolio.

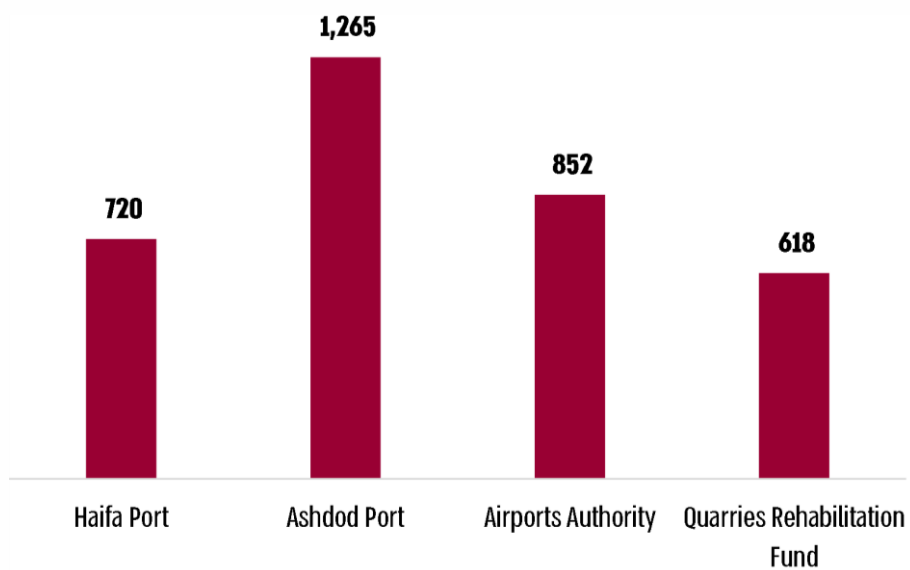
### Total investments portfolios of the institutional bodies in millions of NIS in 30.6.20



Source: data from the said bodies, processed by the State Comptroller's Office.



**Total current investments portfolios of government companies and statutory corporations in millions of NIS in 30.6.20\***



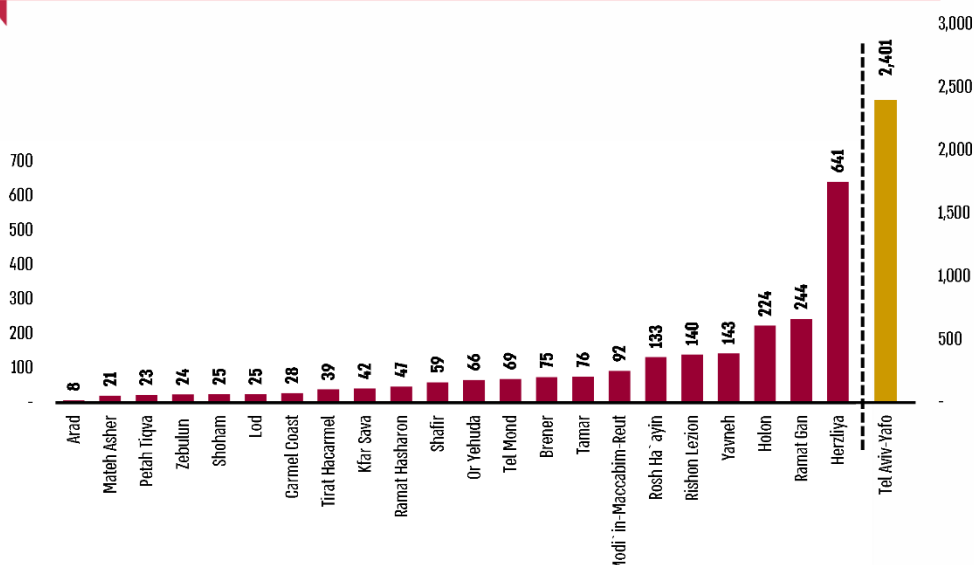
Source: data from the said bodies, processed by the State Comptroller's Office.

\* The Electric Company does not have a current investments portfolio.





### Total long-term investments portfolios of the audited local authorities in millions of NIS in 30.6.20



Source: answers of 50 local authorities to the State Comptroller's questionnaires, October 2020.

## Summary

Rational investment management by local authorities and public sector entities – including determining a suitable investment policy taking into account financial gain considerations or maintaining realistic value of the investment, investment periods and risks – will maximize the inherent benefits of the funds held by the entity. The findings of this report indicate that there are deficiencies in the administrative and professional aspects of the investments committees activities in these entities. Increasing the supervision and control on investments in these entities, among others through the investments committees and educated risk management, is significantly important in times of crisis, where capital markets fluctuations can erode the investments portfolio.





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Systemic Issues

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# **Investments Management at Mifal HaPayis**









## Investments Management at Mifal HaPayis

### Background

Mifal Hapayis (the Israeli lottery) holds lotteries according to a State license given for gambling. Mifal Hapayis designates its profits to assist local authorities in funding health, educational, welfare, cultural and arts projects.

Mifal Hapayis accumulates, on a regular basis, profits that are assigned to projects approved for local authorities and the Ministry of Finance, but the execution of those projects have not yet begun or have not yet completed, taking several years according to project progression. The amounts, which are essentially the commitments of Mifal Hapayis to those projects, are managed by Mifal Hapayis and are invested according to its approved policy.

The total amounts managed by Mifal Hapayis range between NIS 3–4 billion and originate from Mifal Hapayis's gambling profits. These amounts and their annual returns support financing of the aforesaid projects.





## Key figures

**NIS 3–4  
billion**

The total investment funds of Mifal Hapayis from 2017 to 2020.

**-1.18%–  
7.73%**

The range of return on the Mifal Hapayis investments portfolio for the years 2017–2020 (The return derives from the investments policy and the rate of shares in portfolio).

**-2.46%–  
15.54%**

The range of return on the advanced study funds and provident funds in 2017–2020. (The return derives from the investments policy and the portfolio rate of shares – which is higher than the rate of shares in the Mifal Hapayis investments portfolio).

**47%–56%  
of the  
investments  
portfolio**

The scale of investment in government bonds and deposits – a channel that yields low returns on the investments portfolio.

**11%–15%  
of the  
investments  
portfolio**

The scope of investment in shares – a channel that yields high returns from the investments portfolio.

## Audit actions



From December 2020 to April 2021 the State Comptroller has examined the way Mifal Hapayis manages its investments portfolio, and the activity of the entities responsible for outlining the policy and its actual execution; in addition, the supervision and control practices regarding Mifal Hapayis management of investments were examined.






## Key findings

-  **Reference to investments management in the permit given to Mifal Hapayis by the Ministry of Finance** – The Ministry of Finance did not include in the permit any reference to rules of managing the investments, to examination of the method by which the investments portfolio is managed and to implementation of the Board of Directors and Investments Committee directives, to monitoring the portfolio management, to separate accounting presentation of the investments portfolio and to the method by which risks of the investments portfolio are managed.
-  **The Investments Committee** – It was found that despite the fact that Mifal Hapayis investments portfolio totaling NIS 3–4 billion, there is no designated investments committee within Mifal Hapayis and the Finance Committee serves as the investments committee, as allowed in the permit. Whereas the majority of the Finance Committee's activity and resources are not addressed to the investments issue, the matter of managing the investments portfolio – which, as aforesaid, totals approximately NIS 3–4 billion – is an additional subject on the Finance Committee's agenda and not a major issue. The audit also found that, although the Investments committee includes members with financial skills and professional experience from among the board of directors, the Mifal Hapayis Board of Directors procedure determines that most of the Finance Committee members must be able to read and understand financial statements but does not demand financial skills and specific professional experience in the field of investments.
-  **The investments mix and portfolio yields** – The Mifal Hapayis investments portfolio features traditional tools and it has hardly changed over the years. The portfolio yields indicate that during difficult times in the financial markets large losses were caused compared to yields of the benchmark portfolios examined in the audit – which were positive for most bodies (a loss of 1.18% for Mifal Hapayis compared to a range of -2.46% to profits of 2.57% at higher education institutions, provident funds and advanced study funds), and during prolific periods on the markets it showed low results compared with returns achieved in said benchmark portfolios (a profit of up to 7.73% compared to positive returns of up to 15% in the comparative bodies). It should be stated that these returns derive from the Mifal Hapayis policy concerning the investments portfolio compilation that is based on a minimum appetite for risk, particularly regarding the share investment percentage, compared to the policy adopted by the reviewed universities, advanced study funds and provident funds.





-  **Responsible investments (ESG)** – Mifal Hapayis did not hold discussions on the subject of adopting responsible investment rules (ESG). Moreover, the permit given by the Minister of Finance to Mifal Hapayis did not include a reference to this issue.
-  **Risks management** – The semi-annual reports submitted by the risks manager to the Mifal Hapayis management do not include reference to risk derived from investments management.
-  **Investments portfolio management during the Covid-19 pandemic** – The subject of investments was discussed at six out of nine committee meetings held during 2020. During the first half of 2020, a year with many fluctuations in the portfolio yields, the committee discussed the issue of investments at two of the four meetings held. In March 2020, at the time of a large drop in the portfolio yields at a rate of 5%, the Finance Committee did not convene.



**The 2017 internal audit report regarding the investments management of Mifal Hapayis** – This report examined the adherence to procedures and the supervision and control of ongoing investment activities (self-managed activities and those managed by external portfolio managers). The recommendations of the internal audit report were accepted by Mifal Hapayis and implemented in an investments procedure that was approved by the Procedures Committee on January 1, 2018.


**A directive not to invest in bonds of a control owner that did not repay debts to loaners** – Mifal Hapayis decided not to invest in bonds of a control owner that did not repay debts to lenders ("haircut").


## Key recommendations


-  It is recommended that the Ministry of Finance examine the investments management issue and set principles for the Board of Directors investments committee procedures; the considerations for allocating investments to various channels; the method of selecting investments managers; the handling of policy deviations; public transparency concerning amounts in the investments portfolio, investment channels, yields and risk levels.
-  In face of the amount being managed in the Mifal Hapayis investments portfolio, it is recommended that Mifal Hapayis consider establishing a designated Investments Committee, separate from the Finance Committee, that will manage the investment policy, determine the level of exposure to risks and the financial security of the investments portfolio, review investment alternatives and initiate processes; and that the Mifal Hapayis Board of Directors will review updating its procedures to include designated




financial skills and professional experience required from the investments committee members. It is further recommended that the Ministry of Finance appoint, according to its authority, a committee representative with professional training who is not a member of the Board of Directors in order to diversify the committee composition, the opinions heard therein and the decisions it makes.

 It is recommended that those determining the Mifal Hapayis investment policy consider adopting benchmarks for the Mifal Hapayis investments portfolio, and continue to review, from time to time, the investments portfolio composition and entry to additional investment channels available on the market, as a tool for disbursing the portfolio risks and increasing its potential, and as a tool to create security for periods of market fluctuations.

 It is recommended that Mifal Hapayis consider adopting ESG rules ("responsible investments") and integrating them into its investment policy, in view of the extent of the managed portfolio and the positive effects it will have on Mifal Hapayis's public image. It is further recommended that the Ministry of Finance consider including directives concerning adoption of responsible investments rules (ESG) by Mifal Hapayis.

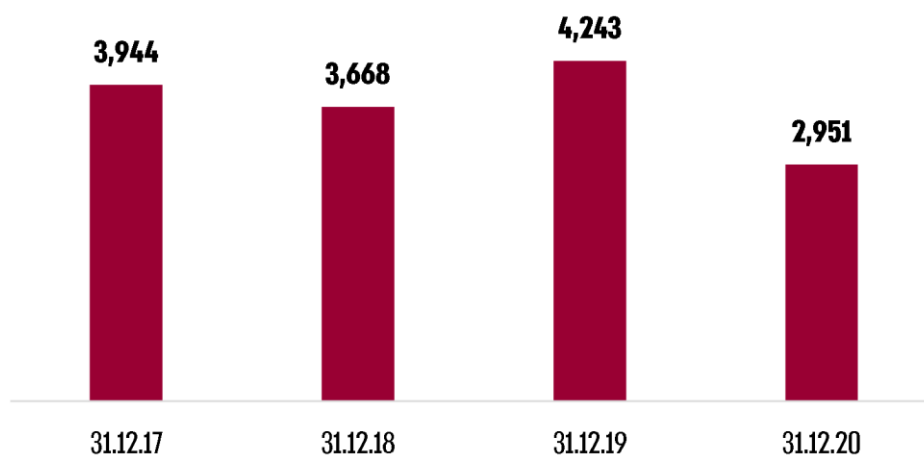
 It is recommended that further to the internal auditor report from 2017 on the subject of investments management, Mifal Hapayis consider formulating for the Investments Committee members a more specific declaration on absence of conflict of interests than the declaration signed by all the Mifal Hapayis directors. Mifal Hapayis should also pay attention to potential affinities between the management of personal investment portfolios and the portfolio managers Mifal Hapayis works with.

 Mifal Hapayis should perform effective risks management of the investments portfolio, submit an annual risks management report to the Mifal Hapayis Finance Committee and Board of Directors and include therein aspects relating to the investments portfolio and management.





### The extent of the Mifal Hapayis investments portfolio, 2017–2020 (in millions of NIS)



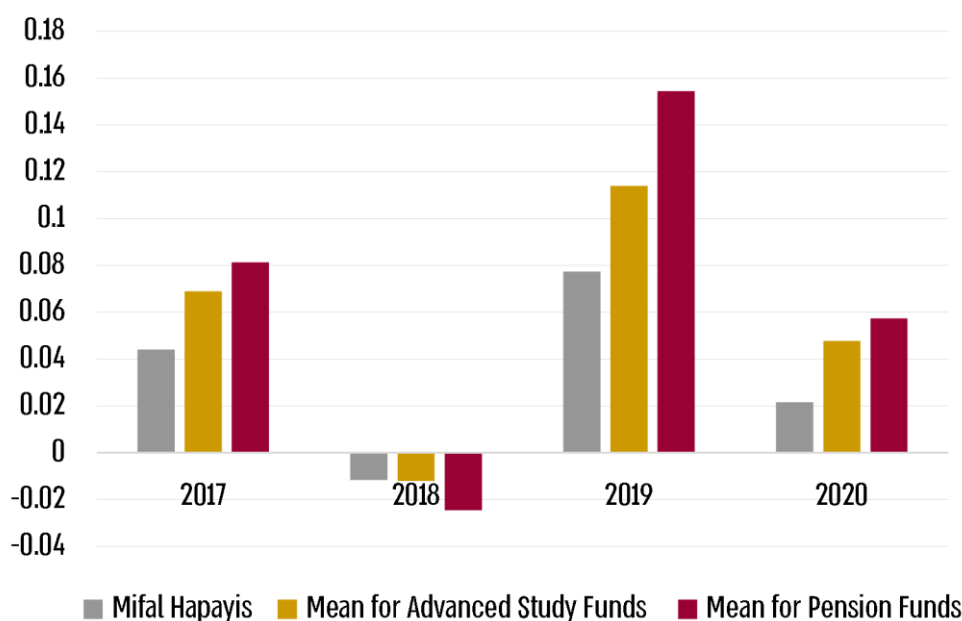
■ Scope of the investment portfolio in millions of NIS.

According to Mifal Hapayis data, processed by the State Comptroller's office.





### The Mifal Hapayis investments portfolio yields compared to the yields of provident funds and advanced study funds, 2017-2020



According to data from Gemel-Net, the Ministry of Finance and Mifal Hapayis, processed by the State Comptroller's office.

## Summary

Mifal Hapayis manages an investments portfolio in a total sum of NIS 3–4 billion (according to 2019–2020 data). These amounts and the annual profits from their yields assist local authorities in financing health, education, welfare, culture and arts projects. Dealing with investments requires professional understanding as well as organized and structured work based on proper control, risk analysis, and transparency between the various factors involved in managing the Mifal Hapayis investments portfolio. Mifal Hapayis should rectify the deficiencies and examine the recommendations raised in this report in order to optimally manage the investments of the funds at its disposal.









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Special Audit Report

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# **Aspects of Umbrella Agreements Signed with Local Authorities**









## Aspects of Umbrella Agreements Signed with Local Authorities

### Background

The significant increase (by 103% in real terms) that occurred in housing prices in Israel from the beginning of 2008 until the end of 2020 increased the weight of the burden on households, particularly for the lower and medium socio-economic levels, and generated a housing crisis. One of the causes for the increase in housing prices is the shortage of housing units. With the intention of encouraging local authorities to promote the development of new residential areas in their jurisdiction and to rapidly market a large number of housing units, the government made a decision in 2013 on the matter of "umbrella agreements with local authorities to remove marketing and development obstructions" (Government decision regarding umbrella agreements). This decision determined that the Ministry of Finance, the Ministry of Construction and Housing (Ministry of Construction) and the Israel Lands Authority (ILA) should contract with local authorities by agreements to develop and market lands within their jurisdiction (umbrella agreements). Since the government decision on the umbrella agreements was made and until end of 2020, 32 umbrella agreement were signed with local authorities – 20 of which signed agreements with ILA and the other 12 with the Ministry of Construction.





### Key figures

**103%,  
34%**

The rate of increase in the housing prices index in real terms from January 2008 until December 2020 and from October 2013, the date the government decision on the umbrella agreement was made and until December 2020 accordingly.

**475,000  
housing  
units**

The number of housing units determined by the government to be included in the umbrella agreements plans to be signed by end of 2020.

**441,000  
housing units**

The number of housing units possible to build on the lands included in the umbrella agreements plans signed with the 32 local authorities, as of December 2020.

**NIS 67  
billion**

Total development costs for the upper and adjacent infrastructures expected in the umbrella agreements signed by January 2020, as of June 2020.

**NIS  
116,000  
per housing  
unit**

The expected average development cost for the upper and adjacent infrastructures for each housing unit in the umbrella agreements, as of June 2020.

**Only  
33%**

The rate of successful marketing of residential lands (in housing units) relative to the marketing rate in the government decision on umbrella agreements, according to the plans apply to the lands.

**Only 7%**

By June 2020 7% of the lands for commercial and employment included in the umbrella agreement plans were successfully marketed (in terms of built sqm).

**98,000  
housing  
units**

The number of estimated housing units in the plans included in the umbrella agreement, that their approval was delayed.





## Audit actions



From March 2020 to January 2021 the State Comptroller examined some of the aspects in the umbrella agreements signed with local authorities in the years 2013–2020. The audit included the rate of adhering to the land for housing marketing capacity, the effects of the umbrella agreements on the financial situation of local authorities, the degree of compatibility between the umbrella agreements and the principles of the strategic housing plans, building permits issued as part of the umbrella agreements and the mechanism to reduce development costs. The audit was conducted at the ILA and Ministry of Construction. Complementary audits were carried out at the Ministry of Finance, the Ministry of Interior, the Government Authority for Urban Renewal (Urban Renewal Authority) and at several local authorities.

## Key findings





**The marketing capacity of lands for housing** – the government decision on umbrella agreements determined that the local authority will undertake in the umbrella agreement to enable the marketing of lands in its jurisdiction at a marketing capacity that will be no less than 2,000 housing units annually (marketing capacity). Hence, as of the second half of 2020, lands that according to the relevant plans can contain 241,000 housing units should have been marketed, had marketing been done according to the determined capacity. The audit found that lands for the construction of only 80,000 housing units had been successfully marketed, which constitute 33% of the lands that should have been marketed had the marketing be done according to the determined capacity, in terms of housing units.



**Integrating urban renewal in the umbrella agreements** – in the government planning goals for 2017–2020 it was determined that planning in the field of urban renewal would extend to 76,000 housing units, around 18% of the total planning for these years (most of which are located in the Tel Aviv, Central, Jerusalem and Haifa districts). According to the Israel Land Council (the Council), the umbrella agreements enabled the ILA to allocate supplementary lands for up to 10% of the housing units in the umbrella agreements for urban renewal, so that the potential is for building up to 44,000 housing units. The audit found that by the end of 2020 only in one of the settlements that signed umbrella agreements, supplementary plots were allocated, as part of a plan that included 3,500 housing units (a plan constituting 0.8% of the total housing units in all umbrella agreements) hence, the agreements did not serve as a main tool for implementing urban renewal projects.






-  **Housing needs of populations in minority communities** – the audit found that in January 2021, the audit completion date, the Ministry of Construction or the ILA had not yet signed an umbrella agreement with a local authority of a minority community, despite the government acknowledged the importance of promoting construction in the minority communities. It should be stated that in September 2021 (after the audit completion date) the ILA signed an umbrella agreement with the Um-El-Fahm municipality.
-  **Housing needs of the ultra-orthodox population** – despite the need to build 200,000 housing units for the ultra-orthodox population from 2016–2035, as of the audit completion date no ultra-orthodox neighborhoods had been marketed in any heterogonous city that was included in the umbrella agreements, according to the government decision regarding housing for the ultra-orthodox community from August 2016. It was found that in three local authorities, neighborhoods designated for the ultra-orthodox community are in various planning stages, totaling 2,350 housing units (in Ramla and Netivot) as well as in Acre as part of the "Acre Gates" 8,000 housing units plan for the general population. At the audit completion date these plans had not yet been marketed. Moreover, despite more than four years have passed since the government decision was made, the Ministry of Construction and the Budgets Department at the Ministry of Finance have not yet formulated a system of incentives to include neighborhoods for the ultra-orthodox population in the umbrella agreements.
-  **Reporting on implementation of the government decision on umbrella agreements** – the government decision on umbrella agreements did not determine any system of reporting on the implementation of the decision. Moreover, during 2013–2020 the Council did not discuss failure to fulfill the marketing capacity or the obstructions preventing it. Furthermore, the audit found the annual statements for 2013–2019 submitted by the ILA to the Council including a report on the umbrella agreement signed in the relevant years, and sometimes even included details of the number of housing units marketed and a report on agreements expected to be signed. However they did not include any report on obstruction to implementing the agreements or on the disparity between the actual marketing and the marketing capacity as determined by the government decision on the umbrella agreements.
-  **Marketing commercial and employment areas as part of the umbrella agreements** – as of June 2020 only 7% per the lands for commerce and employment included in the umbrella agreements plans were successfully marketed, in terms of built-up sqms. For over half of the local authorities that signed the umbrella agreements by the end of 2017 (13 out of 25) the rate of lands for housing successfully marketed (by housing unit) out of the lands included in the agreement plans was greater by 10% and more than the rate of successfully marketed lands for commerce and employment (by sqm of built-up area according to the plans) out of the total lands for commerce and employment included in the agreement plans. Due to the fact that the local authorities relied mostly on their expected revenues from collecting business municipal fees, which




may affect the local authorities financial situation and their ability to provide their residents with an appropriate level of services.

 **The rate of building permits and the duration for their issue** – the rate of building permits of the total housing units included in the agreements plans with 11 local authorities audited was from 7% in Beer Yaakov to 58% in Rosh Ha'Ayin, which was one of the first local authorities to sign the umbrella agreement. On average building permits were issued for 23% of the total housing units included in the umbrella agreement plans for the 11 audited local authorities. The duration for receiving building permits at ten of the audited local authorities was over 90 days as determined by the umbrella agreement. The duration for receiving a building permit ranged from 132 days in Netivot to 504 days in Netanya, and on average 309 days. It should be noted that the duration for receiving permits depends on various factors, including the applicants submitting the request and those who edit it, and the circumstances some of which are not in the local authority's control. It was further found that the umbrella agreements grant at the amount of NIS 129 million, was given to local authorities that signed the umbrella agreements during 2019 and 2020 according to indexes relating to population growth in the local authority and not according to the number of building permits issued by the local authority, despite the Ministry of Interior's program being "a program of incentive to local authorities to issue building permits for housing units". As a result the grant did not serve as an incentive for these local authorities to issue building permits.



**Savings on development costs** – the results of ten tenders to perform development works, as part of the umbrella agreements audited, indicated that an accumulated saving of NIS 157 million (24%) on the estimated costs of these works, was achieved through these tenders.

## Key recommendations

 It is recommended that the ILA and the Ministry of Construction monitor how the local authorities are fulfilling the marketing capacity of housing units as determined in the decision on the umbrella agreements, conduct joint strategic work to map out obstructions and difficulties of each of the umbrella agreements realization steps and act together to formulate proposals to remove these obstructions and overcome the difficulties. It is recommended that representatives of relevant entities, including government ministries and companies whose involvements are required as well as representatives of the Local Government, be included in this process. It is further recommended that the results of the process be presented to the Minister of Construction and Housing, discussed by the Council and if necessary alternative solutions be formulated to promote the government objectives for providing solutions to housing requirements. It is further recommended that the Minister of Construction and Housing





convene the Council from time to time to discuss the implementation of the umbrella agreements, and convene the Ministerial Committee for Housing and Transportation to examine the possibility of establishing a mechanism for reporting to the committee or the government on the implementation of the government decision on umbrella agreements. It is also recommended that as part of the decision making process on the extent of housing units to be marketed in each local authority, the development costs and land values be analyzed and the possibility of setting a basic development cost be examined based on coefficients relating to land conditions and other relevant variables.



It is recommended that the Ministry of Construction, the ILA and the Ministry of Finance, together with the Ministry of Interior, examine individually how realization of the umbrella agreements may affect the local authority's financial situation and its ability to provide an appropriate level of municipal services to its residents, including examining the feasibility of marketing and realizing lands for commerce and employment and the ability to rely on revenues from the derivative business municipal fees. In compliance with the examination findings it is recommended that the Ministry of Construction, the ILA and the Ministry of Finance formulate an appropriate response required for the local authority due to realization of the umbrella agreement and possible affect to its financial situation as a result of realizing the umbrella agreement. It is further recommended that the Ministry of Interior and Ministry of Finance, together with local authorities, the Ministry of Construction and the ILA, examine ways of promoting marketing and realizing lands for commerce and employment in their jurisdictions to increase their revenues from business municipal fees. It is further recommended that the Ministry of Construction and the ILA formulate objectives for marketing commercial and employment lands in all local authorities that signed the umbrella agreements.



It is recommended that the Ministry of Construction and the ILA examine, together with the Urban Renewal Authority, possible ways for promoting urban renewal projects in local authorities that signed the umbrella agreements, particularly in cases where the land value is too low for creating financial feasibility and formulate a multi-year plan that will enable the local authorities to fulfill the housing unit objectives regarding urban renewal planning.



It is recommended that the Ministry of Construction and the ILA act together with government ministries and other State authorities and together with the relevant local authorities to promote the signing of umbrella agreements with local authorities of minority communities, in addition to the agreement signed with the Um-El-Fahm municipality in September 2021.



The Ministry of Construction and the ILA should promote marketing of housing units for the ultra-orthodox population in all relevant local authorities that signed umbrella agreements, according to the government decision of August 2016 on that matter. Moreover, the Ministry of Construction and the Budgets Department at the Ministry of Finance should complete formulating a system of incentives to motivate local authorities





of heterogeneous communities signed on umbrella agreements to include ultra-orthodox neighborhoods in the agreements, according to the government decision on housing for the ultra-orthodox population.



It is recommended that if the Ministry of Interior and the Ministry of Finance decide to continue distributing grants to local authorities as incentives for issuing building permits, the process will include an examination of the conditions for receiving these grants. This should be done in order to make these grants an incentive to the local authorities for issuing building permits, particularly in view of the data indicating that the local authorities issued a smaller rate of building permits than required and the extensive duration required for their issue.

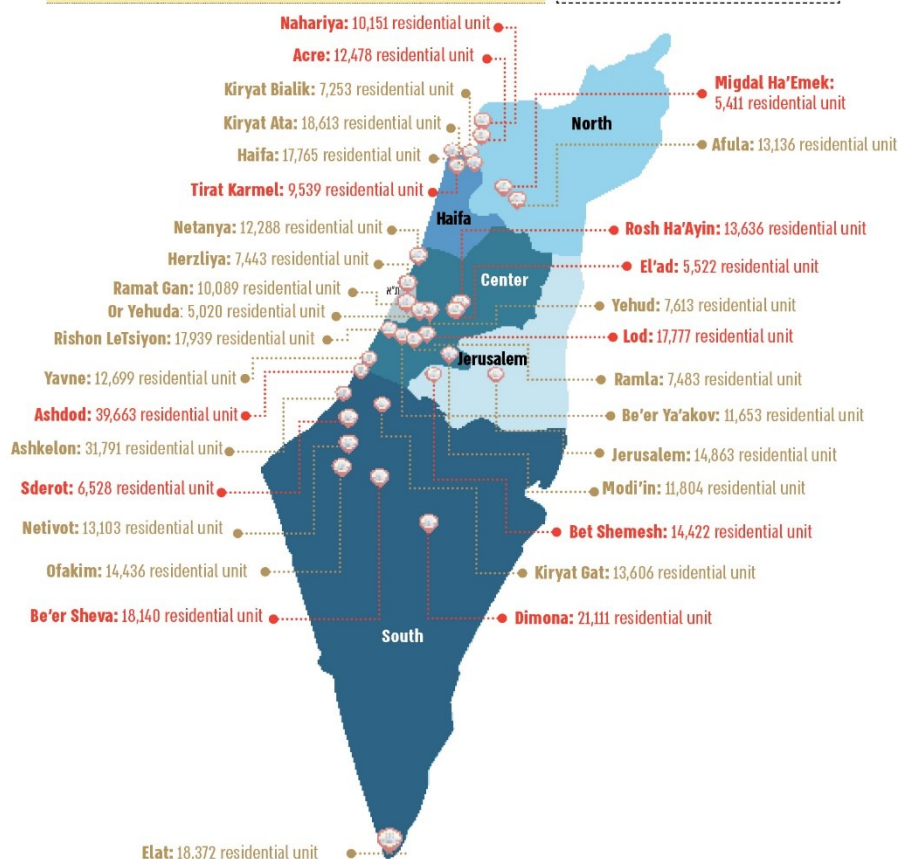




## Communities for which an umbrella agreement has been signed, and the number of housing units in the plans in each agreement

District	Total housing units in the agreements	Their share out of the total housing units in the agreements	Their share out of the target set by the government
South	176,750	40%	37%
Center	123,434	28%	26%
Haifa	53,170	12%	11%
North	41,176	9%	9%
Jerusalem	29,285	7%	6%
Tel Aviv	17,532	4%	4%
Total	441,347	100%	93%

Attributed to the Ministry of Construction and Housing  
Attributed to ILA



According to the ILA and Ministry of Construction and Housing data, as processed by the State Comptroller's Office.





## Summary

From January 2008 until December 2020 the housing prices index increased by 103% in real terms; and from October 2013, the date the government decided to promote the signing of umbrella agreements with local authorities, the index increased by 34%. The umbrella agreements signed over recent years are heavily resourced complex land development and marketing agreements, that regulate the main framework for the development and construction of large scale housing projects for the coming years. The umbrella agreements signed in the years 2013–2020 were designed to create a "toolbox" for the large scale construction of housing units – with plans for 475,000 housing units by the end of 2020 – at a marketing capacity of 2000 housing units annually at each of the 32 local authorities that signed the umbrella agreements by the end of 2020, while decreasing the negative incentive of local authorities to increase the number of housing units in their jurisdiction. In fact, the umbrella agreements were meant to be a central tool for fulfilling the housing requirements of Israel's population, whereas the strategic plan requires the planning for 2.6 housing units and the construction of 1.5 million by 2040.

The audit indicated that difficulties and obstructions during the planning, development and marketing phases make it difficult for local authorities to fulfill the marketing capacity, and in fact by the end of 2020 land for a total of 80,000 housing units had been marketed in all local authorities, constituting an average of 33% of the expected marketing capacity. As a result the government will not be able to address Israel's housing requirements. The audit also found that as of the end of 2020 employment areas totaling 1.3 million sqm were marketed out of a total 17.6 million sqm employment areas included in the umbrella agreements plans (constituting 7% of the total areas included in the agreements). Significant additional housing construction without sufficient added sources of income, and particularly business municipal fees, may affect the ability of the local authorities to provide a proper level of services for the residents in the future.

In view of the above, it is recommended that the ILA and the Ministry of Construction monitor how the local authorities are fulfilling the marketing capacity of housing units as determined in the decision on the umbrella agreements, hold joint strategic work to map out obstructions and difficulties at each of the realization phases of the umbrella agreements and act together to formulate proposals to remove the mentioned above obstructions and overcome the difficulties. It is further recommended that the results of the process be presented to the Minister of Construction, be discussed by the council and if necessary – alternative solutions be formulated to promote the government objectives for providing solutions to housing requirements.

It is also recommended that the Ministry of Construction, the ILA and the Ministry of Finance, and the Ministry of Interior, examine how realization of the umbrella agreements may affect the local authority's financial situation and its ability to provide a proper level of municipal services to its residents, and according to the examination findings, formulate a solution





required for the local authority as a result of realizing the umbrella agreement. It is further recommended that the Ministry of Interior and the Ministry of Finance, together with local authorities, the Ministry of Construction and the ILA, examine ways of promoting the marketing and realization of lands for commerce and employment in their jurisdictions to increase their revenues from business municipal fees.





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## Chapter 2

# Government Offices









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Ministry of Energy

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# **The Benefits from the Implementation of the Gas Outline**







## The Benefits from the Implementation of the Gas Outline

### Background

In 1999 and 2000 the natural gas reservoirs – Mari-B and Noa were discovered off the coast of Ashkelon. These reservoirs are part of the Tethys Sea project, the size of which is BCM 34 and from which gas was produced until 2019. Additional natural gas reservoirs were discovered between 2009–2013 in Israel's exclusive economic zone, including: "Tamar", "Tamar South-West", "Dalit", "Leviathan", "Karish" and "Tanin". To regulate the State's share in the gas profits, the Petroleum Profits Taxation Law was passed in April 2011 (its name was later changed to the Taxation of Profits from Natural Resources Law 2011), determining that the gas project will pay a levy on Petroleum profits. The share of the State in the gas profits is comprised of royalties imposed on revenues from gas sales, the Petroleum profits levy and income tax that applies to the profits of holders of rights in the gas reservoirs. In view of the limited number of bodies holding rights to search for and produce natural gas, and their need to cooperate due to the high investment costs required, cross ownerships on the gas reservoirs were formed as well as and monopolies of holders of gas rights. From 2011–2015 the Israel Competition Authority acted to reach an agreement with holders of the rights for gas exploration and production regarding the restrictions that would apply on them, in order not to affect the competition in this field. During these years, in the absence of consent and in the absence of regulatory certainty, the Leviathan, Karish and Tanin reservoirs were not developed. Government Decision 476 of 2015 approved "the outline for the increase of natural gas supply from Tamar gas field and fast development of Leviathan, Karish and Tanin and other natural gas reservoirs" (the Gas Outline) as agreed with the rights holders in the gas reservoirs. This framework determined, among other things, the reservoirs development schedule, ensuring redundancy in supplying gas and the structural change concerning ownership of the gas rights and provided holders' regulatory stability.





## Key figures

**NIS 4.2  
billion**

Revenue from income tax (including additional taxation due to the Israeli Tax Authority assessments) for gas projects, from 2011 to 2018.

**NIS 7.8  
billion**

State revenues from gas and Petroleum royalties from 2004 to 2020.

**Only NIS  
741  
million**

Accumulated amounts from the levy on profits from natural resources between 2011 and June 30, 2021. (Compared to the Bank of Israel forecast of 2013, which stood at over NIS 1.7 billion by the end of 2020).

**NIS 200  
billion**

Estimation of the amount to be received from the levy on profits from natural resources until 2064.

**NIS 57.4  
billion**

Evaluation of the amount to be received from Petroleum and gas royalties from 2020 to 2064.

**2 operators**

And a mix of different ownerships in each of the three gas reservoirs.

**3 reservoirs**

Are expected to produce gas during 2022, the gas will flow to the national gas system through three different systems.

**134 BCM**

Approved for export to Egypt and Jordan.

## Audit actions







From October 2020 to February 2021 the State Comptroller's Office examined the implementation of the Gas Outline and the benefits achieved following its implementation. The first part of the report reflects the findings and recommendations regarding the development of competition in the gas market in view of the affect the competition has on this market due to actions by some of the rights holders of the gas discoveries, the effect of the Gas Outline on the redundancy in supply of gas to the Israeli economy, gas export and the promotion of foreign and security relations. The second part reflects the findings and recommendations regarding the collection processes of oil and gas royalties, the oil profits levy and income tax. As part of the audit, various actions of the Ministry of Energy, the Israel Competition Authority and the Israeli Tax Authority were examined. Supplementary examinations were conducted at the Ministry of Finance,



the Accountant General Department, the Bank of Israel<sup>1</sup>, the Ministry of Justice, the Israel Electricity Corporation Ltd. (IEC), the Electricity Authority, the Government Companies Authority and the natural gas production companies.

## Key findings

-  **The purchase of gas from other suppliers by IEC following the "Leviathan" agreement** – the Competition Authority did not provide any reference as to whether the agreement between the IEC and the "Leviathan" partnership is a prohibited binding settlement affecting the competition law or does not adhere to the conditions determined by the Gas Outline. Therefore the agreement between IEC and Leviathan came into effect.
-  **The Gas Framework and development of the "Tamar South-West" field** – two years following the mediation agreement between the State and the reservoirs rights holders, the parties are still negotiating the share of the State in the profits from the future sales of the gas produced. The Accountant General Department and the Ministry of Energy are cooperating on matters of the engineering aspects of the reservoir development. At the same time, the audit found that the Accountant General Department has not yet examined the form of supervision over the "Tamar South West reserve", as required by the Outline, because there is no agreement regarding the entity that should be in charge of collecting the State's share.
-  **The State's share in revenues from the gas discoveries – an international comparison** – in December 2018 a team headed by the Ministry of Energy CEO completed an examination of the developments that occurred in the Israeli gas market during the five years since the government decision, and conducted a renewed examination of the supply and demand for natural gas, including resources, reserves and a current and future status of natural gas reservoirs development. However, the audit found that the team did not examine world developments over the years on the subject of taxation and did not examine Israel's position regarding this matter in comparison to the situation in countries of this region in particular and in the world in general.
-  **The handling of gas projects by the Tax Authority** – the Income Tax Assessor for Large Enterprises T-A deals with the Taxation of Profits from Natural Resources Law, and examines cross cutting issues in the gas project. Sometimes those issues affect income tax assessment of all rights holders in the project under examination and for

1 The Bank of Israel has been appointed as responsible for investments and management of reservoirs accrued in a fund for the wellbeing of Israel's citizens (the Wealth Fund).





other projects. Dividing the gas reservoirs rights holders between various income tax assessors requires additional resources for training, guidance and findings sharing. It was found that all rights holders in the "Leviathan", "Karish" and "Tanin" reservoirs were grouped under the Income Tax Assessor for Large Enterprises, but not all of the rights holders in the "Tamar" reservoirs were grouped, one of its rights holders is assessed for income tax in Haifa.



**Sharing information between the Ministry of Energy and the Tax Authority –**

the Taxation of Profits from Natural Resources Law determines four subjects on which the Income Tax Assessor is obliged to consult with the Ministry of Energy commissioner before making decisions that are significant for the levy coefficient or the levy imposed on a petroleum project. Up until the audit completion date the method of sharing information between the Ministry of Energy and the Tax Authority remained unresolved. The Ministry of Energy did not take the necessary steps for sharing information and ensuring cooperation despite being addressed on this matter by the Tax Authority over the years 2016–2020. Moreover, the Ministry of Energy did not provide the Tax Authority with a written document detailing the conditions requiring fulfillment as part of the process of discovery recognition of project, the conditions and procedures for granting holding approval as well as information requested by the Tax Authority regarding one of the holdings. All these may influence the relevant determinations for calculating the levy coefficient and the date and scope of levies the project will actually be required to pay.



**The dates of declaring a discovery and granting possession of the gas discoveries –**

despite the fact that results of the "Leviathan" drilling were published at the end of 2010, the Ministry of Energy determined the discovery date as January 2014. This required the Tax Authority to examine the possibility of defining a different date for conclusion of the search period rather than the date determined by the Ministry of Energy for rights holders of the gas reservoirs, and required the sorting and classification of the reported results for search expenses and establishment expenses. Incorrect sorting and classification affect State revenues from gas receipts. It should be noted that during the postponement period between 2013–2014 the "Leviathan" rights holders spent hundreds of thousands of NIS that, in their opinion, should be considered as expenses attributed to the search period that are entitled to benefits, until possession is granted according to the Taxation of Profits from Natural Resources Law.



**Forecast of Wealth Fund revenues<sup>2</sup>** – opposite to the forecast given in 2013 by the then Bank of Israel Governor for the beginning of the Wealth Fund activities in 2018 (after the accrual of a billion NIS) and the forecast according to which by the end of 2022 the fund will have accumulated approximately USD 3.9 billion, the amount the fund has accrued, as of June 2021 was only NIS 741 million.

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<sup>2</sup> See the Fund for Israeli Citizens Law, 2014 (Fund for Israeli Citizens – Wealth Fund).










**Gas reservoirs infrastructures** – During 2022 three gas reservoirs are expected to be connected to the Israeli economy through three separate infrastructures, owned by three groups comprised of different ownerships, in order to reduce to some extent the centralization of the gas market and improve redundancies.

**Exporting gas** – Exporting gas has awarded the State of Israel certain advantages in the regional and international political-security area, and may promote normalization in relations with countries in the region, contributing to Israel's foreign relations.

## Key recommendations

-  It is recommended that the Competition Authority examine the contracts regarding gas sales of gas reservoirs submitted for its approval and consider the conditions they include, and whether they contain any breach of the Gas outline or of competition terms, as determined by the Competition law and not exempted by the government decision regarding the Gas Outline.
-  After the agreed order enabling rights holders in Tamar to sell gas from the reservoir separately was being approved in June 2021, the State Comptroller's Office recommends that the Competition Authority monitor quotations by the rights holders for gas sales, and examine all possible actions should any concern arise of price coordination between the rights holders in the "Tamar" and "Leviathan" reservoirs.
-  It is recommended that the Accountant General Department and the Ministry of Energy complete formulating the way for monitoring "Tamar South-West" reservoirs and reach an agreement regarding the appointment of an entity in charge for collecting the State's share. It is further recommended that the Accountant General Department complete the negotiation on all matters pertaining to the implementation of the mediation agreement concerning the proceeds.
-  It is recommended that the Ministry of Energy monitor from time to time the policy accepted worldwide for determining the rate of countries share in gas profits so that it will be prepared in advance to update Israel policy upon completion of the government's commitment for regulatory stability, determined in the Gas Outline as 2025. This should be done with transparency, with combination of additional tools and while maintaining feasibility of exploration for new gas reservoirs and gas production. It is further recommended that the Ministry of Energy and the Tax Authority determine methodology for calculating and publishing annually updated rates of the State's share in the revenues from gas discoveries.
-  It is recommended to establish a joint team of the Tax Authority and the Ministry of Energy (approved by the Minister of Finance) for monitoring the levy and gas profits





coefficient and to complete an agreed procedure for consultations between the Ministry of Energy and the Tax Authority. It is further recommended that this team examine the possibility of determining uniform reporting, as much as possible for both entities, in order to reduce bureaucracy, improve the efficiency of the monitoring process of the share in revenues owed to the State and to prevent gaps and mistakes.



It is recommended that the Ministry of Energy recognize a discovery and determine the possession date according to the earliest possible date when commercial production becomes feasible, independently of the actual date of submission of documents, and no later than the date of submitting the application for discovery and possession. This date matches the reduction in the project's financial and engineering risk level, as described in the explanation to the Taxation of Profits from Natural Resources Law.

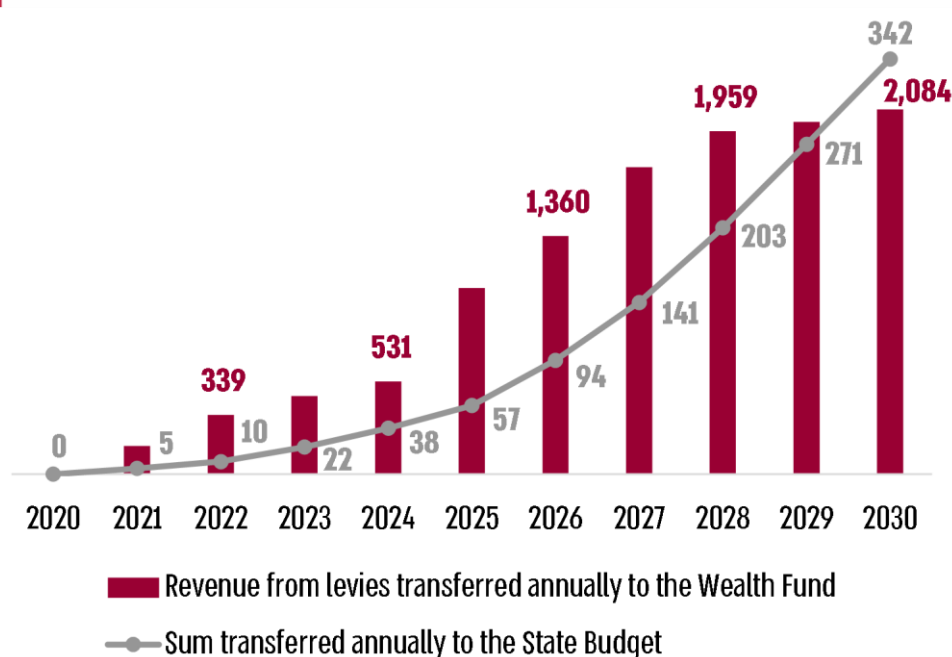


The Tax Authority should complete its examination of all matters pertaining to resolving the collection of taxes on nature profits, in view of the disparities discovered and accumulated experience, including examination of the search period. Amending the regulation will decrease the differences of opinion between the projects rights holders and the State and will reduce the possibility of postponing tax payments.





**The forecast of revenues from the levy on profits from natural resources and the funds that will be transferred to the State budget, every year, until 2030 (in millions of USD dollars)**



The source: data of the Tax Authority as presented to the special committee for supervising the fund for management of State revenues from the levy on gas and oil profits, July 28, 2020, processed by the State comptroller's office.

## Summary

The natural gas economy is facing major challenges and has several regulators. In face of the variety and complexity of the issues at hand, the large amounts in question and the effect each of these issue have on other relevant issues, it is highly important that the various regulators formulate rules of cooperation between them. Despite over a decade have passed since the discovery of the natural gas reservoirs, the main regulators responsible for developing the gas economy and maintaining the State's financial interests, have not succeeded in formulating an agreed and coordinated work procedure that will contribute to assuring an appropriate share of the State from the gas production.





The findings raised in this report indicate that some of the objectives for which the Gas Outline was formulated have been achieved. Three gas reservoirs have been developed and during 2022 three separate entries connected to the national gas system are expected to operate, in addition to the LNG import buoy. Moreover, an additional operator will begin supplying gas to the economy, thereby reducing cartelization. This will greatly improve redundancies on the gas market. However, during the audit period according to the principles determined in the Gas Outline, there are still cross holdings between the rights holders of the gas reservoirs and there is one operator for both reservoirs, which may affect the sections in the competition law that have not received exemption within the Gas Outline. As of June 2021, the sum of NIS 741 million (as of 2019 – NIS 474 million) has been accrued in the Wealth Fund, compared to the Bank of Israel forecast delivered in 2013, according to which an amount of NIS 1.7 billion was expected to accumulate by the end of 2020.

The gas economy has significant effect on the economy, industry, on energetic security and on Israel's political resilience. Therefore, the Ministry of Energy, the Tax Authority, the Competition Authority and others must cooperate in the relevant areas, in order to ensure utilization of the potential inherent in this resource, including the need to increase the wealth of the public funds.





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Ministry of Economy and Industry  
Israeli Standards Institute

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# **The Standardization Reform**







## The Standardization Reform

### Background

A large portion of Israel's economy is based on the import of products and services. Israel trades in a wide range of products, and imports a large portion of production inputs, consumer products and investment assets.

In 2000, the Ministry of Finance and the Ministry of Economy & Industry noticed that Israeli standards create non-tariff barriers (not customs related) on imports to Israel, thereby restricting competition and limiting the range of products available to consumers. This is leading to higher prices for many products. Accordingly, the Standardization Law 1953 was amended. The Israel Standards Institute would, generally adopt international standards<sup>1</sup> accepted in developed countries, when determining its standards.

Over the years, various committees were established to resolve the problem of the bureaucratic burden in the import process and the use of official standardization as an import barrier and to ease the financial burden imposed on Israel's citizens.

In 2016–2017 amendments to the Standards Law were enacted which were known as the "standardization reform". The amendments were designed to make the Standards Institute activities more efficient, and award the Standardization Commissioner the authority to authorize additional testing laboratories for imports. These changes were intended, among others, to reduce costs, shorten the timeframe for announcing obligatory standards updates and to improve service quality. The reform further determined a mechanism for expedited examination of non-binding national changes in obligatory Israeli standards.

The Institute is a public entity established under the Standards Law 1953, with three authorized laboratories working alongside it in 2020<sup>2</sup>. They test imported goods for adherence to the requirements of the applicable required standards.

<sup>1</sup> Concerning technical regulation, including standards or international regulation-based regulations.

<sup>2</sup> A laboratory endorsed by the commissioner for performing tests over imported goods for compatibility with the official standard according to the Import Export Ordinance (New version) 1979.





## Key figures

### **30,000 voluntary standards**

The number of voluntary international standards published by the ISO and IEC standards organizations. Compared to only 3,500 standards published in Israel.

### **USD 307 and 64 hours**

The average cost of adapting import documents in Israel and the duration of the process, compared to USD 98.1 and 8.5 hours on average in the OECD countries in 2020.

### **USD 70 and 44 hours**

The average cost of customs tests in Israel and duration of the process, compared to USD 23.5 and 3.4 hours on average in the OECD countries in 2020.

### **Only 3 private laboratories**

The number of private laboratories endorsed for testing imported goods in 2020.

### **2% only**

The percentage of recommendations regarding laboratory test reports<sup>3</sup> of imported goods requiring testing that were issued by private laboratories from May 2019 to September 2020, compared to the rate of almost 98% of recommendations issued by the Standards Institute.

### **37**

Staffed positions of the 54 available positions in the Standards Administration in 2020.

### **42**

The number of endorsed laboratories<sup>4</sup> in 2019.

### **approx. NIS 19 million**

The cost of standard adherence tests for ceramic tiles (monopolistic area) in 2019 for approximately billion released items.


<sup>3</sup> At the conclusion of testing, the laboratory provides the standards commissioner with a recommendation of whether to release the goods for marketing or not.

<sup>4</sup> A laboratory registered by law as a corporation in Israel, with the professional capacity and skills, prepared to fulfill its duty as a laboratory in Israel for approvals, according to the terms and directives provided by the commissioner for this matter.



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## Audit actions

 From August 2020 to January 2021, the State Comptroller's Office performed an audit of the standards reform. The audit focused on the following subjects: implementation of the reform by the Ministry of Economy; the improvement in service and the increase in competition; the Standards Commissioner's functioning; early retirement of Standards Institute personnel according to a special collective agreement; promoting new reforms in 2020; and computerized data systems for goods imports. The audit included a public participation procedure survey of several importers and authorized private laboratories on the standards reform subject. The purpose of this procedure of the survey was to examine the effect of the reform on importers' work from various aspects of the import process, including the financial aspect, the professional aspect and the services offered by the Standards Institute and the private laboratories that entered the activity as part of the steps for opening the area to competition. The public survey was performed through interviews with seven officials in Israeli companies that deal with import and marketing in various areas. These included some of the leading and largest importers in the market, that operate with an import volume totaling billions of NIS annually, and others, smaller that operate or specialize in limited areas and import tens of millions of NIS annually. The audit was conducted in the Standards Administration of the Ministry of Economy. Supplementary examinations were conducted in the Standards Institute, the Ministry of Finance, the Competition Authority and the Israeli Tax Authority.

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## Key findings

-  **The efficiency of importing goods to Israel compared to OECD countries –** Indexes measuring document processing and customs testing of imports, import times and costs in Israel were several times higher than the OECD average. It takes more time for Israeli importers to import goods and the cost of testing during the import process is higher. Moreover, the relative situation in Israel compared to the OECD average worsened from 2015–2020: for example, in 2015 the costs of Israel's import tests were 250% higher than the costs of import tests in OECD countries, and in 2020 this difference had increased to 300%.
-  **Improvement of services to importers –** The Standards Commissioner has no data on the time elapsed from the moment of importers submit requests to the laboratories until they issue test results, or the amount of time required for laboratories to handle the importers' requests for test. In addition, no documentation was found of the tests performed by the Commissioner on service quality. From May 2017 to May 2019 there was a 10% improvement at the Standards Institute in the rate of testing orders processed within a week. The average number of days until testing orders were





processed decreased from 10 to nine. It should be noted that the Standards Institute executed 60% of the testing orders within two days during 2018–2019.



**Adapting obligatory national standardization to international standardization**

– Amendment 13 to the Standards Law was enacted two and a half years ago and required an examination of existing obligatory standards and their adaptation to international standards by August 2019. Nevertheless the examination of 115 obligatory standards (approximately 30% of the standards to which Amendment 13 applies) has not yet been completed. These standards had been referred to the Ministry of Economy's Commissioner for Import Legality for examination. He in turn submitted them to the Ministry of Finance for approval. As of May 2021, the audit completion date, approval was received for one standard only. Because the Ministry of Finance considers that there are national deviations that remain in these standards that should not be included in the obligatory standards, it has not approved them.



**The Ministry of Economy RIA<sup>5</sup> report from 2016**

– The Ministry of Finance and the Ministry of Economy have not examined if the expected savings to the economy following the legislation amendments cited in the RIA report have materialized. This examination is important in view of the agreement that the Ministry of Finance signed in 2017 with the Institute, whereby the Ministry of Finance undertook to finance 80%–90% of the early retirement costs of 300 Institute employees. Following this agreement, 140 of the Institute employees took early retirement by November 2020 at a cost of NIS 264 million, of which the Ministry of Finance covered NIS 219 million.



**Achieving the standardization reform objective to increase competition**

– Despite that three years have passed since the imported goods testing market opened for competition, the percentage of tests performed by private laboratories is negligible – only 1.1 % of all tests and 2% of the standards that were opened to competition. This compared to the Standards Institute, which is still performing almost all of the tests. As of September 2020, the Standards Reform had not succeeded in achieving its basic objectives.



**The Standardization Administration supervision activities**


– In 2020, only 36 of the 54 positions at the Standardization Administration were staffed. The number of inspections performed by the Standardization Administration to enforce the obligatory standards in 2019 (around 1,700) was 0.56% of the number of test laboratory reports for the same year (over 300,000). It was also found that the number of inspections to enforce the obligatory standards dropped from 2,300 in 2017 to 1,700 in 2019. In addition, the Standards Commissioner does not impose monetary sanctions on importers that breach any of the Import and Export Ordinance directives. The number of product


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5 Regulatory Impact Assessment (RIA) Report.




return recalls published on the subject of standardization dropped from 34 in 2017 to 20 in 2019.

 **Imposing monetary sanctions** – In January 2021 the Ministry of Economy had not yet completed preparations for imposing monetary sanctions according to the Import and Export Ordinance and the Standards Law and therefore did not utilize its authority to impose monetary sanctions.

 **The process of submitting online applications** – The Customs "Maslul" (Route) system connects importers, exporters, customs agents and government authorities. However, the data regarding applications submitted by importers to the Institute via Maslul was transferred to Customs and the Commissioner in PDF format, which cannot be computer, processed. This makes risk analysis difficult since in this format processing the importer application data is impossible. Moreover, private laboratories were not connected to the customs "Maslul" computer system. This made it difficult for the Tax Authority to perform risk assessment in order to decide which goods should be sampled.

 **Findings of the public participation procedure – importers and endorsed laboratories** – The public participation procedure survey of importers and private laboratories raised several issues. Service to importers has improved for standards for which there is competition between testing laboratories. The private laboratories are not yet attractive enough for the importers due to various impediments. The Standardization Commissioner should encourage competition and as much as possible, introduce additional authorized testing laboratories to the field. The Institute should invest funds in upgrading its equipment and its technological development.

 **Promoting new reforms in 2020** – The 2020 RIA report estimated that performing the proposed changes would save NIS 210 million annually for importers, which would reduce prices for consumers by an estimated NIS 420 million annually, whereas the estimated cost of maintaining the existing situation was an additional NIS 900 million for consumers. As of the audit completion date, the Settlements Law and the State Budget for 2020 had not yet been completed and the reform had not yet been approved.



**Defining new national standardization** – In January 2021 it was more difficult for interested parties to announce a new obligatory standard that included unnecessary national changes, since Amendment 12 of the Standards Law determines that this procedure requires the consent of the Minister of Finance and the Prime Minister.







**Actions to fill supervisory positions** – The Ministry of Economy, the Ministry of Finance and the Civil Service Commission have commenced action to upgrade employment contracts for inspectors in the Ministry of Economy. During the audit period, formulation of employment contracts for inspectors in the standardization administration was completed, and most of the inspectors have signed the new contract.





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## Key recommendations

-  It is recommended that the Ministry of Finance, the Ministry of Economy and the Standardization Commissioner continue to act to improve Israel's import indexes to the level of OECD averages. The Ministry of Economy and the Standardization Commissioner should adopt a target of increasing the number of voluntary standards in Israel thereby providing a response to market requirements, including compilation of a list of standards appropriate for adoption and a multi-year plan for their adoption, with emphasis on adopting international standardization.
-  Further to Amendment 13 of the Standards Law regarding completion of obligatory standard reviews by August 2019, the Ministry of Finance and the Ministry of Economy should complete the handling of obligatory standards that are in dispute. It is recommended that the Ministry of Economy formulate a mechanism for reaching a decision when there is a disagreement between the standards adoption committees and the Ministry of Finance. In the absence of such a mechanism, the disputes should be submitted to the Prime Minister's Office CEO, and if the dispute is a legal matter, then it should be brought before the Attorney General.
-  It is recommended that the Ministry of Finance and the Ministry of Economy examine whether the RIA 2016 assessments concerning the expected savings to the economy materialized and what impediments prevent their realization, particularly for implementing the RIA 2020 report.
-  The Ministry of Economy should adopt a systematic, timely procedure for examining improvements in service quality according to the goals of the Standards Law amendment. It should fully document the work process and retain its findings, in order to contribute to service improvement.
-  It is recommended that the Ministries of Finance and Economy examine what impediments prevent an increase in the number of private laboratories that test standard performance of imported goods and take action to augment the share of private laboratories performing these tests. In addition, the Ministry of Finance, the Ministry of Economy and the Standardization Commissioner should continue examining alternatives for exemptions to the import regulation procedures. They should consider the new infrastructure used in Europe and the policy practiced in the USA and other countries, and examine Israel's import policy in a timely manner with international comparisons.
-  It is recommended that the Ministry of Economy Standardization Commissioner increase control and enforcement operations to maintain effective supervision designed to locate goods where the importer's declaration of compatibility to obligatory standards is



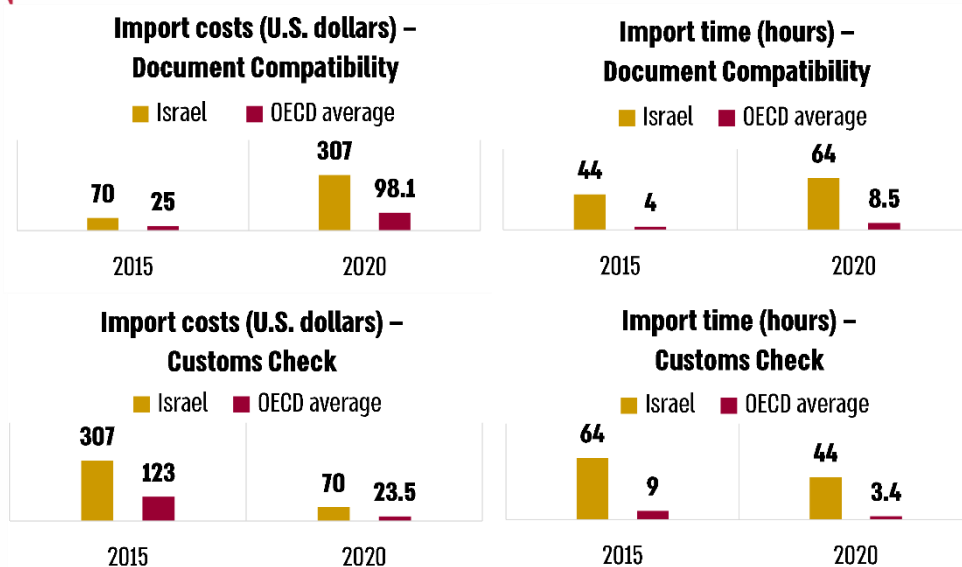
incorrect. It is further recommended that the Standardization Administration at the Ministry of Economy act to complete its preparedness for imposing monetary sanctions and exercising its powers.



The Standardization Commissioner and the Customs Administration at the Tax Authority should act to develop improvements in the "Maslul" system so that importers' applications can be transferred in computer compatible files, reach agreements that will enable private laboratories to connect to the system and complete defining the model for detecting suspicious deliveries at the early stages of import.

### Duration of importing goods<sup>6</sup> to Israel and its costs compared to the average in OECD countries.

The import efficiency measures for time and cost in two categories – adapting documents and customs checks for imports – in Israel compared to the OECD countries average for 2015 and 2020.



According to Doing Business data for 2020, processed by the State Comptroller's Office.

<sup>6</sup> Acquiring, preparing and submitting documents during transportation, approval, testing and handling at the port or border of the originating country. Acquiring, preparing and submitting documents required by the destination country's economy and the transition country's economy. Including all the documents required by law and in fact, including submission of electronic data.





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## Summary

The standardization reform, designed to generate change in this sector, did not achieve its major objective. At the time of writing this report, there was very little competition from private laboratories. The Ministries of Economy and Finance recognized this fact, and since July 2020, they have been promoting an additional actual reform in standardization, making the previous reform devoid of any content. It was found that the reform did not deal with the process of testing the goods, including the process for receiving regulatory approval required for importing prior to marketing of the goods and its adjustment to the practices of developed countries. Therefore, the regulatory burden on importers that entails sample testing of the imported goods and deliveries, has improved only slightly. The public participation procedure regarding the reform, including importers and authorized laboratories, as performed by the State Comptroller's Office, showed that regarding standards where there is competition among authorized laboratories and the Standards Institute, the service and prices given to importers are better and more competitive. The State Comptroller's Office recommends that the Ministry of Finance and the Ministry of Economy continue to act towards increasing competition in the field of testing for adherence to standards, and increase the market share of tests performed by endorsed laboratories. They should take steps to remove impediments to approving authorized and approved laboratories to the field. They should also reduce the regulatory burden on importers in order to lower the cost of living and expand the variety of available goods, while maintaining vigilance and assuring that all goods entering the State's ports adhere to obligatory standards and do not present any hazards to public health.





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Ministry of Transport and Road Safety

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# **Providing Accessibility in Public Transportation to Persons with Disabilities**









## Providing Accessibility in Public Transportation to Persons with Disabilities

### Background

The commitment of the society in Israel to ensure the rights of persons with disabilities is based on acknowledging the principle of the equal rights, the value of all human life and human dignity<sup>1</sup>. Public transportation is vital for persons with disabilities, enabling them to be independent, have access to employment services, education and health and to integrate into society. Adapting the physical and human environment to physical, sensory, emotional and cognitive abilities of persons with disabilities will improve their functioning.

1 Article 1 of the Equal Rights for Persons with Disabilities Law 1998





### Key figures

**1.56  
million**

The number of persons with disabilities in Israel (of which 1.2 million are aged 20 and over).

**17%**

Of the general population in Israel are persons with disabilities.

**50%**

Of persons with disabilities do not work<sup>2</sup>.

**33%**

Of the persons with disabilities population travel by city buses daily. 15% of the persons with disabilities population travel daily by intercity buses.

**NIS 2.4  
billion**

The estimated direct government expense in 2017 on mobility for passengers with disabilities (according to the Joint survey).

**875**

Accessible taxis operating currently in Israel out of the 1,000 licenses distributed around Israel.

**85**

Settlements in which 1,000 and over residents do not have an accessible possibility to physically travel by public transportation from their place of residence to other settlements.

**NIS 3.9  
billion**

The Ministry of Transport cost estimate of providing accessibility in all intercity bus services<sup>3</sup>.

## Audit actions



From September 2020 to March 2021 the State Comptroller's Office examined the subject of providing accessibility in public transportation to persons with disabilities, and among others, arriving at the pick-up point, the accessibility of stations and of means of transportation. The audit was conducted at the Ministry of Transport and Road Safety (the Ministry of Transport). Supplementary audits were performed at the Commission of Equal Rights for Persons with Disabilities at the Ministry of Justice (the Equality

<sup>2</sup> According to a survey conducted by the Joint in 2019.





<sup>3</sup> According to the Ministry of Transport data that was presented to the Knesset Data and research Center in 2017, as processed by the State Comptroller's Office.





Commission), at Egged transport Company Ltd, at Dan Public Transportation Company Ltd and at the Israel Railway Company Ltd. The audit included a public participation process, within which participation meetings were held with dozens of organizations and NGO's, with public representatives and with activists and other relevant entities.

## Key findings

-  **Travel difficulties in public transport** – a survey conducted by the Joint in 2019 indicates that most persons with disabilities of all kinds (around 60%) are not satisfied with the existing accessibility solutions in public transportation. The survey further indicates that passengers with cognitive or physical disability or sight disability experience difficulties during most of the travel by public transportation, whereas persons with hearing disability or emotional disabilities have difficulty in leaving their home, in waiting for the travel and in travel itself. Accordingly, there is only a low number of persons with disabilities that use the various transportation services compared to the general population.
-  **The absence of obligation in the Equal Rights for Persons with Disabilities Law 1998 to provide accessibility in inter-city buses** – even though the law was passed in 1998, at the time of the audit completion date, the law had not yet included an obligation to provide physical accessibility in inter-city buses. Moreover, the insight survey and the public participation process indicated that the obligation for sensory accessibility in buses as determined by the regulations (PA system, electronic data) is not completely fulfilled and there are flaws in its implementation.
-  **The cost of accessing inter-city buses** – according to the Ministry of Transport estimate, the total costs required for accessing inter-city buses is NIS 3.9 billion for 12 years. The Ministry of transport evaluation refers to the accessibility process of all inter-city buses, and does not refer to the possibility of partial accessibility, i.e. in some of the routes or some of the operating hours of the buses or by coordination in advance, and particularly routes that do not have parallel train lines. Partial accessibility should decrease costs.
-  **Accessibility of city buses** – a survey conducted by the Ministry of Transport raised deficiencies in the accessibility of city buses which resulted in the need to improve the accessibility in several major areas: (a) adapting the service to persons with disabilities including, among others, encouraging bus drivers to act respectfully and thoughtfully and train them to be aware of the difficulties persons with various disabilities deal with and be considerate of them. (b) ensure the use of accessibility means such as: stopping as nearby to the curb as possible, using lowering means and ramps, beginning to drive after wheel chairs are secured and operating public address systems. (c) response time adherence by public transportation operators to complaints concerning accessibility to





persons with disabilities and ensuring the availability and response of an accessibility officer representing the public transportation operators. (d) Reducing bus ticket costs for people that accompany persons with disabilities. At the time of the audit completion date the Ministry of transport had not prepared a comprehensive and detailed program for handling this matter, and there was no reference to the issue of training the drivers in the Ministry of Transport's supervision reports.



**Providing accessibility of bus stations and access routes to the stations** – in 2019 there were approximately 27,000 bus stations in Israel. As of that year there were still 13,500 inaccessible city stations and 3,500 intercity- service stations that are not accessible. In 37.5% of the 80 examined settlements not all the stations are accessible and in 22.5% of the examined settlements, less than 85% of the stations are accessible. Moreover, at the audit completion date, almost 16 years since the date of amending the Equal Rights Law, the Minister of the Interior has not yet legislated regulations for accessible routes.



**Ministry of Transport supervision** – the Ministry of Transport did not require the public transportation operators to provide information regarding the publication of accessible routes, on installing static signs and on handling of public complaints. The audit also found that the Ministry of transport did not require the Local Authorities to submit a list of accessible bus stations; moreover, the National Public Transportation Authority did not issue a semi-annual report concerning bus stations that provide city services, and at the Public Transportation Accessibility department in the Ministry of Transport no received reports on this matter were found.




#### **Israel Railways Accessibility**


- **Coordinating travel for persons with disabilities** – according to the train travel coordination procedure, a person with disability wishing to travel by train should coordinate his travel two hours in advance with the company's service center. The audit found that the number of persons with disabilities able to travel at the same time is limited to the amount of coordinations and the type of the disability. The audit also found that for most of the coordinated travel the departure stations are in the center of the Israel, whereas the amount of coordinated travel at peripheral stations is low.
- **Height differences between platforms and railway carriages** – there are height differences between the platforms and the stair at the passengers entrance to the railway carriages. These differences are significant for passengers in wheelchairs as well as passengers aided by other mobility aids.
- **Sensory accessibility at train stations** – in six out of eight stations examined in the audit complete sensory accessibility was found in all the passenger elevators, in the ticket offices and in all other public areas. However, at the Ashdod Ad-Halom station and the the Tel Aviv elevators, the PA system designed to assist persons with






sight disability in their orientation and movement between floors in the station was not working.

 **Accessible taxis** – in Israel 1000 licenses for operating accessible taxis have been issued, providing a ratio of one accessible taxi per 1,600 persons with disabilities, compared to one taxi per 340 passengers without disabilities. In reality, at the audit completion date, 875 accessible taxis are active. Moreover, despite the corporations having been awarded a discount of 95% in the fees payment (NIS 10,000 instead of NIS 240,000) deficiencies were found in all matters pertaining to the collection of high traveling fees and failure to document travel records. Complaints were received that the accessible taxis serve in fact as transportation vehicles and therefore are not available for persons with disabilities seeking to order an accessible taxi. It was further found that the issuing licenses process was done without determining any criteria or threshold requirements, where any entity seeking such licenses was awarded the license based on the quantity of licenses allocated by the Ministry of Transport for this purpose. After receiving the franchises, and even after the various operators began providing services, the Ministry of Transport did not formulate any contract or agreement with the operators to regulate their liabilities and rights concerning provision of this service.


 **Geographical distribution of the licenses for accessible taxis** – a review of the 19 corporations holding public rights indicates that seven corporations are in the Jerusalem area, four in the Tel Aviv and central area and six in additional areas. This data shows that for most corporations the license validity will expire within five years of the audit completion date.

 **The price of travel in accessible taxis** – despite the corporations having been awarded a 50% discount in the fee payment, deficiencies were found in all matters pertaining to the collection of high tariffs and of failure to keep travel records.



**Accessibility at train stations** – the audit examined eight train stations – in most stations there is convenient and adjusted access to disembarkation areas near the station entrances and parking lots, the entrance lobbies or checkpoints. In all stations examined there are visual marking for passengers from embarkation and disembarkation points in all passenger halls and up to the station entrance.

## Key recommendations

 It is recommended that the Ministry of Transport complete comprehensive examination of all aspects regarding public transportation of persons with disabilities, including mobility habits, the obstructions preventing their use of public transportations and the reasons for their immobility. Accordingly, it is recommended to formulate a proposal for





ways of government intervention that will ensure consideration of all persons with disabilities including the matter of technological developments.



It is recommended that the Ministry of Transport include in its supervision program mechanisms for monitoring the behavior and training of drivers, to ensure greater accessibility to persons with disabilities by the service providers. It is further recommended that the Ministry of transport examine the need for updating regulation regarding the accessibility of public transportation services, including determining training procedures and contents, and update the directives to bus drivers and other service providers of public transportation and monitor their implementation; all this in order to improve service regarding the interface between drivers and persons with disabilities using public transportation.



It is recommended that the Ministry of Transport and the Equality Commission act to promote the matter of accessibility regarding intercity transportation, examine this matter compared to solutions practiced in other countries worldwide, and propose operative actions for activating accessible intercity transportation, including performing a pilot if necessary.



It is recommended that the Israel Railway hold public participation processes among persons with disabilities, from time to time, to learn of the disparities they show and to formulate a program to improve these matters and examine solutions for the difference between the railway carriages and platforms and improve service coordination in the periphery.



It is recommended that the Ministry of Transport set an agreement with operators of accessible taxis defining the rights and duties required thereof as part of operating franchises for accessible taxis, will act to prevent sale of licenses before ten years from the license receipt date will pass and set a procedure that will ensure awarded licenses are indeed used for the transportation of persons with disabilities.

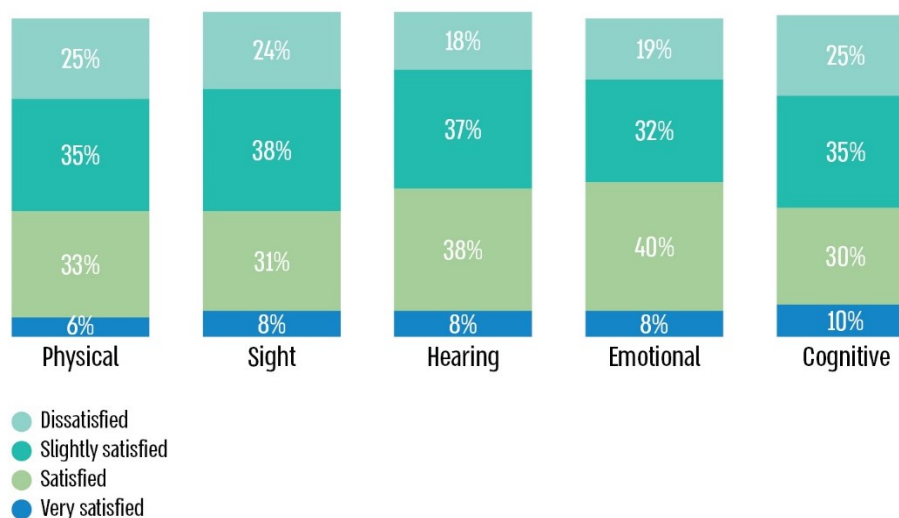


It is further recommended that the Ministry of Transport, together with the Equality Commission, taxi associations and NGO's that deal with accessibility matters for passengers with disabilities, examine ways of providing high availability of accessible taxis for persons with disabilities throughout Israel in general, and in the peripheral regions in particular.





### Satisfaction with accessibility solutions, according to type of disability



The source: Joint survey of 2019.

## Summary

In Israel there are almost 1.5 million persons with disabilities constituting 17% of the total population, and over 20% of the adult population aged 20 and over are persons with disabilities (1,176,600). Many have to contend with low incomes (75% are persons with severe disability) and with difficulties in financing monthly expenses (19% of persons with severe disability and 11% of person with moderate disability), in owning and maintaining a car (63%) and in obtaining a driver's license (60%). An additional difficulty is to the ability to use transportation in order to travel independently. Adapting the physical and human environment to the physical, sensory, emotional and cognitive abilities of persons with disabilities coincides with the principle of equal rights for persons with disabilities and is an important step in the process of enabling independent, respectable and equal lives in the community while contributing to their mobility. Improving the traveling Possibilities of persons with disabilities provide extensive financial benefits, such as social and financial mobility for persons with disabilities, new employment possibilities, saving costs of special transportation, expanding possibilities for receiving vital services and increasing productivity in the economy.









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Ministry of Transport and Road Safety

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# **Operation Agreement with Egged and its Structural Change**







## Operation Agreement with Egged and its Structural Change

### Background

The majority of public transportation services in Israel are provided by buses – a sector that in the past was dominated by two cooperatives – Egged and Dan. In July 2019 the Egged cooperative became a private company – Egged Transport Company Ltd. (Egged). Egged operates bus lines by power of edicts, agreements and licenses awarded by the Ministry of Transport and Road Safety (the Ministry of Transport) as part of its role as the regulator of public transportation. Since the beginning of the 21st century, the Government has been promoting a reform designed to improve public transportation services by increasing competition. As part of the reform, several agreements have been signed over the years between the State and Egged. The purpose of these agreements was to enable gradual release of transport lines to competition and to allow Egged a period of reorganization in order to improve its preparedness for changes in the sector. Egged's operational costs are higher in comparison to the operational costs of the competitive operators, therefore as part of these agreements the Government subsidizes from the State budget Egged's excess operating costs. In November 2018 the State and Egged signed an operation agreement, applied retroactively from the beginning of 2016 and which is valid until 2029. The agreement deals with the issues of promoting competition in the sector, raising service standards and Egged's efficiency process. The agreement provides Egged with a long-term program and incentives for increasing efficiency and preparing to operate under competitive conditions. The agreement includes releasing approximately 27% of the Egged lines to competition during the agreement period (and, together with the lines released according to the previous agreement, a total of 33%) and releasing the remaining lines at the end of the period. In addition, the agreement includes the issue of retiring senior employees and implementing efficiency procedures; setting measures for improving service standards; regulation of the use of infrastructures owned or managed by Egged by other operators; altering the ownership and incorporation structure including turning Egged into a limited company; and payment of 25% of the Company's monetary value to the State.





## Key figures

**NIS 10.2 billion**

The total operating cost of public transportation in buses in 2019.

**NIS 2.5 billion**

Egged's annual operation costs, as determined by the agreement (without participation in purchasing).

**32%**

Egged's portion in the bus public transportation sector in 2020, in terms of travel distance, compared to 75% pre-reform and compared to the 25% target at the agreement termination date (2029).

**NIS 1.3 billion**

Estimated value, as of 2018, of Egged shares received by the cooperative members upon its becoming a company.

**14 years**

The operation agreement period.

**NIS 400 to 700 million**

The range of evaluations of the gap between Egged's annual operation costs including the purchase of buses and the retirement of senior employees in comparison with the competitive operators. The gap derives also from cluster characteristics.

**NIS 868 million**

The State's portion in financing the retirement costs of senior Egged employees in the agreement period.

**NIS 181 million**

The average annual participation of the State in the purchasing costs of Egged buses for 2016–2020.

## Audit actions



From September 2020 to May 2021 the State Comptroller's Office audited the signing process of the operation agreement between the State and Egged, its implementation and the supervision and control by the Ministry of Transport on adherence to its terms. Egged's financial performance and its operating efficiency were also examined. The audit was performed at the Ministry of Transport and Egged. Complementary audits were performed at the Budgets Department and the Accountant General Department in the Ministry of Finance.



## Key findings



**Releasing Egged lines to competition** – the Ministry of Transport has not yet released the lines operated by Egged for competition according to the operation agreement, and there is a risk that it may not complete releasing all Egged lines by the end of the agreement period, end of 2029. The audit found that in order to fulfill the goal of Government decision 4148 to release all Egged lines for competition by 2030, the Ministry of Transport will have to publish over 20 tenders from 2027–2030. Over recent years the Ministry of Transport has published two to three tenders annually.



**Egged's operational efficiency** – Egged has not fulfilled all of its commitments and goals set by previous agreements. At the beginning of 2019 its operational efficiency was still low compared to other operators, mainly due to high personnel costs and use of an old vehicle fleet, and its operation costs for city and intercity clusters were high. According to the State Comptroller's Office estimate, the cost per km travel by Egged in 2019 was approximately 30% higher for city services and 10% higher for intercity services, compared to competitive operators.



**Egged's financial performance** – in 2016–2017 during which there was no valid agreement between the State and Egged, most of the company's financial performances (profitability, financial resilience and liquidity) were lower than the multi-year average. For example: there was a sharp drop in gross profit and in EBITDA; the debt ratio to EBITDA in 2016 was 2.6 times higher than the ratio in 2010 and 3.2 time higher than the 2019 ratio; the immediate liquidity ratio in 2018 was defiantly lower compared to the average in 2010-2019. Therefore, Egged received retroactive payments from the State at the time of signing the operation agreement.



**Egged's long-term financial forecast** – Egged has provided the Ministry of Transport with a forecast for the agreement period, and presented an efficiency program. Egged also presented the effect of the efficiency program and the outline for the release of lines to competition on its profitability and operation costs. At the same time, the forecast did not show the effects on balance sheet items and cash flows and did not include sensitivity analyses.



**The involvement of the Ministry of Transport and the Ministry of Finance in preparing Egged's valuation** – although the State is entitled to a payment of 25% of Egged's rights, the Ministries of Transport and Finance were not involved in Egged's preparations towards the company's value estimate.





**Government financing for employee's retirement** – according to the operation agreement the government participates in the retirement financing costs for employees






due for compulsory retirement, which comprises an additional benefit to Egged and does not constitute an incentive for efficiency. The government portion in financing retirement costs totaled NIS 868 million during the agreement period.

 **Granting company shares without payment to Egged members** – at the time of changing the form of incorporation, the Egged members received a commitment for payment of the full value of their shares in the cooperative and company Ltd. shares without payment. The company shares' value is estimated at NIS 1.3 billion according to an estimate as of 2018. These actions were taken without the involvement of the Ministries of Transport and Finance.

 **Regulating the use of public transportation facilities** – the Ministry of transport did not issue licenses for transportation facilities that were supposed to deal with terms for holding and operating the facilities, including the issue of shared use by different operators, despite the shortage of such facilities and their necessity for operating public transportation services.

 **The Ministry of Transport supervision of the standards of services by Egged** – the Ministry of Transport calculates a score for measuring the service standards of operators which serves as one of the criteria for selecting tender winners. For many years Egged was not entitled to bid for tenders to operate service lines, and therefore the mentioned score had no effect on its chances for winning future tenders; therefore, the incentive the score provided Egged to adhere to the predefined service standard was weak compared to competitive operators. This situation remains the same as long as Egged is not entitled to bid for tenders to operate service lines. Moreover, the Ministry of Transport's supervision of the service standard that Egged provides along a travel route is unsatisfactory. For example, in 30% of the total bus fleets there is a passenger counting system that enables checks during travel, but the Ministry of Transport does not yet use it to monitor crowding in buses.








Since the beginning of the reform in public transportation over the past two decades, new operators have entered the sector of public transportation, and they are operating service lines by virtue of winning competitive procedures.

Over the years Egged has improved its efficiency in certain aspects, among others due to retirement of senior employees and changing the nature of employment in the company, as well as by increasing the number of drivers while decreasing the number of administrative workers.



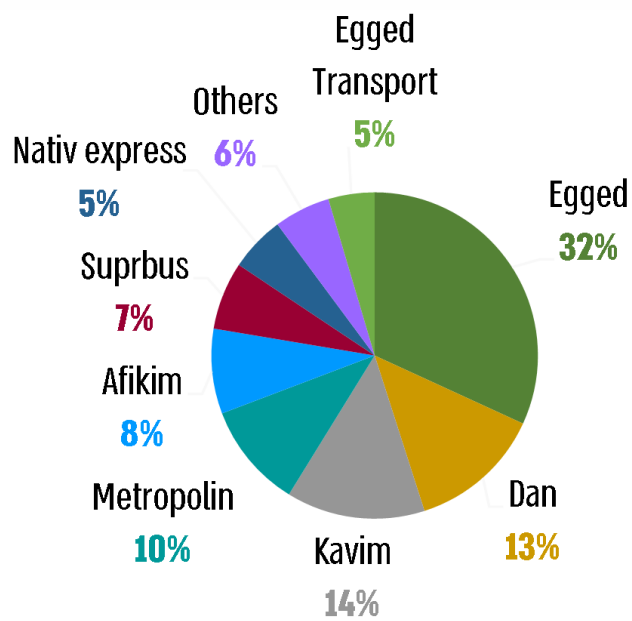
## Key recommendations

-  It is recommended that the Ministry of Transport prepare in advance a multi-year program that includes goals and milestones for releasing the remaining lines operated by Egged to competition, in order to prevent continued financing of Egged's excess costs out of the State budget.
-  It is recommended that the Ministry of Transport monitor Egged's activity regularly to ensure implementation of the operation agreement and continue to develop means for supervising adherence of public transportation operators to all requirements determined in their agreements.
-  It is recommended that Egged expand the financial forecast presented to the Ministry of Transport to include the aspects of balance sheets and cash flows as well as various scenarios concerning the retirement forecast and the operational forecast to enable defining the steps to be taken so that at the conclusion of the agreement period the company's expenses structure will enable it to contend with a competitive market without needing the State to finance its excess costs. It is further recommended that Egged set efficiency goals and formulate a multi-year plan to stabilize its financial coverage and leverage ratios in order to improve its financial resilience and fully prepare it for competition. It is recommended that the Ministry of Transport examine the efficiency goals formulated by Egged and monitor their realization in order to verify that the company improves its financial resilience and prepares for competition.
-  It is recommended that the Ministries of Finance and Transport examine the implications of granting company shares without payment to the founders on the company's financial situation, taking into consideration the payments the State has transferred to Egged, and be involved in the various processes of changes in the corporate or the organizational structure of the Company, so as to verify that its members are not being given excess proceeds without examining the implications.
-  It is recommended that the Ministry of Transport examine means for realizing its authority to promote shared use by different operators regarding the use of public transportation facilities and create a mechanism for supervising management of the facilities in order to enable efficient use that will support competition. It is also recommended that the regulation of the transfer of the facilities to management of public entities or local authorities be examined.





**Market shares in the bus public transportation sector, by distance traveled, 2020 (in percentage)**

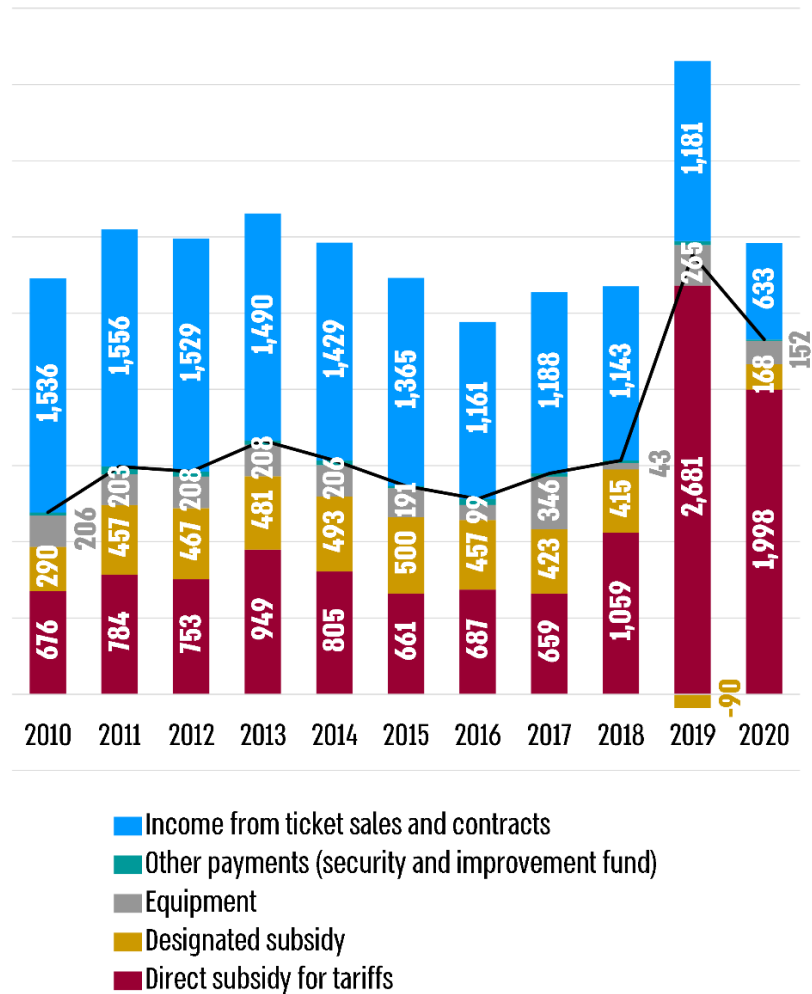


According to Ministry of Transportation data, processed by the State Comptroller's Office.





### Egged incomes for 2010–2020 (in millions of NIS)



According to Ministry of Transport and Egged data, as processed by the State Comptroller's Office.





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## Summary

Since the beginning of the 21st century the government – through the Ministry of Transport – has been promoting a reform to improve public transportation services and increase competition in the sector. At the audit completion date, Egged remains the largest operator in the sector, and its market share in terms of distance traveled was 32% as of 2020. Egged has become more efficient over recent years, but at the beginning of 2019 its personnel costs and operating costs of its service lines were still high compared to competitive operators, and it continues to be dependent on receiving subsidies from the State, which also covers its excess costs. The State Comptroller's Office recommends that the Ministry of Transport prepare in time for release of the remaining lines operated by Egged to competition, in order to fully implement the reform in public transportation according to the determined schedules. In addition, the Ministries of Finance and Transport should monitor Egged's fulfillment of its obligations according to the operation agreement, particularly in terms of standards of service provided to the passengers and its efficiency procedures. Egged should prepare for the conclusion of the agreement period the structure of its expenditures will enable reasonable profitability and capacity to contend with a competitive market without needing the State to finance its excess costs.





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Ministry of Transport and Road Safety

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## **Public Transportation – Use of Rav-Kav Cards (Follow-up Audit) and Payment Applications**









## Public Transportation – Use of Rav-Kav Cards (Follow-up Audit) and Payment Applications

### Background

The Rav-Kav card is a reusable rechargeable electronic card – was entered into service in 2007 to the Dan region, and its use was gradually expanded to all around Israel and to all public transportation operators. A significant portion of travel payments for public transport are made using the card. For each of the years from 2016 to 2020 there were an average of 3.5 million active Rav-Kav cards (an active card is defined as being used at least once during the recent six months of that calendar year).

The State Comptroller's Office conducted a follow-up audit regarding the rectification of the deficiencies raised in the previous audit published in 2017<sup>1</sup>. The main deficiencies mentioned in the previous audit included among others deficiencies concerning the issuing and recharging of Rav-Kav cards, deficiencies in the recovery of Rav-Kav cards and receiving refunds, deficiencies in the validation and charging of Rav-Kav cards and deficiencies in contracting to operate a service center and in backing up its data.

1 State Comptroller, **Annual Report 68a** (2017) "Use of Rav-Kav Cards in Public Transport", pp. 425–454.





### Key figures

**3.5 million**

The average annual number of active Rav-Kav cards in 2016–2020.

**Approximately 891 million**

The number of travels in all public transportation existing in 2019.

**NIS 9.2 billion**

The total subsidy received by public transportation operators in 2019.

**770 million**

The number of bus travels in 2019, which are 86% of all public transportation travels (buses, Israel Railway, light rail, etc.) for that year.

**5% to 23%**

Estimation of the rate of public transportation users that avoid paying for travels.

**NIS 300 million**

The Ministry of Finance estimate of the expected loss in the State Budget for each year following the avoidance of payment for travels.

## Audit actions



From September 2020 to January 2021 the State Comptroller's Office conducted a follow-up audit regarding the rectification of the deficiencies raised in the previous audit (the follow-up audit or the current audit). The current audit examined the following subjects: the Ministry of Transport preparedness for cyber events concerning the database of Rav-Kav users, and the use of applications for public transportation services, commenced on 15.12.20. The audit was carried out mainly at the National Authority for Public Transportation. Supplementary examinations were performed at the Privacy protection Authority at the Ministry of Justice (the privacy Protection Authority), at the Ministry of Public Security and the IDF.





## Key findings



**Regulating supervision and enforcement authorities for unpaid or unvalidated travel** – the previous audit stated that expanding the use of open systems (Rav-Kav validation systems that are not adjacent to or involve the driver) requires activating appropriate enforcement measures to ensure validation of cards as required and accuracy of the reports regarding the number of passengers. The follow-up audit indicated that although legislation procedures have begun to amend the Transportation Ordinance [new version] in 2018, the legislative regulation of supervision and enforcement powers on public transportation regarding unpaid or unvalidated travels. The follow-up audit showed that the deficiency on this subject was only slightly rectified.



**Determining extended tariff for unpaid or unvalidated travels** – the previous audit stated that the Ministry of Transport should examine the possibility of determining various extended tariffs, and should consider differentiating between an unpaid travel by the passenger, and a paid but unvalidated travel. The follow-up audit found that no change occurred in the extended tariff amounts imposed by all public transport operators compared to their amounts at the conclusion of the previous audit. Therefore the absence of differentiation between an unpaid travel and a paid but unvalidated travel remained. The follow-up audit further found that the Ministry of Transport has not completed the examination of this issue. The follow-up audit indicated that the deficiency regarding this issue was not rectified.



**Regulating the use of Rav-Kav cards** – the previous audit stated that the legislative procedure to regulate the use of Rav-Kav cards had been ongoing for many years, and therefore the Ministry of Transport should examine how to promote this procedure. The follow-up audit indicated that the legislative procedure has not been completed, including the issues of users rights, of issuers activities, and the enforcement authority and the assurance of protecting the privacy of Rav-Kav users, despite the fact that ten years have already lapsed since the bill on the subject was prepared by the Ministry of Transport (in 2010). The follow-up audit found that the deficiency regarding this issue was not rectified.



**Protection of Privacy of Rav-Kav card users** – the previous audit stated that the subject of protecting the privacy of Rav-kav cards users had not yet been specifically legislated, and therefore the directives of the Law, Technology and Data Authority at the Ministry of Justice (currently the Privacy Protection Authority) for the interim period as determined in April 2012, was still valid after five years. The follow-up audit showed that regulating the application of the Protection of Privacy Law 1981 directives on the databases storing the data on Rav-Kav card holders has not yet been completed, and





that the Law, Technology and Data Authority at the Ministry of Justice directive published in April 2012, is still valid, even though over eight years have passed since its publication. The follow-up audit showed that the deficiency regarding this issue was not rectified.



**Backup of the service center** – the previous audit stated that "there is no backup site for the Rav-Kav cards setup, only for the data, which increases the risk of affecting the services provided to passengers the revenues following an attack or fault at the service center". The previous audit also stated that "in the discussion held in June 2016 the Authority Manager repeated the warning of the importance of establishing backup site for the service center". The follow-up audit found that the subject is being handled by the Ministry of transport, which published a tender in January 2021 for the provision of services for public transportation users holding Rav-Kav cards. The follow-up audit indicated that the deficiency regarding this subject was only slightly rectified.



**Recovery of Rav-Kav cards and receiving refunds** – the previous audit stated that card holders entitled to refunds or that require recovery of their cards must sometimes wait 72 hours from the time of applying to the service station until the full recovery is possible. The follow-up audit found that passengers can recover travel arrangements immediately except for travel arrangements paid for 72 hours prior to recovery. After this time passengers can immediately recover these travel arrangements as well. The deficiency therefore has been rectified to a great extent.

**Expanding service stations (service centers)** – since publication of the previous audit additional service stations have been established, including two virtual stations where actions on the Rav-Kav card can be performed independently. Moreover, the layout of existing recharging stations (estimated at thousands) for Rav-Kav cards has been expanded around Israel.

**Payment using cellular phones** – the Ministry of Transport acted to enable payment for public transport travel using cellular phones from mid-December 2020, in addition to payment by Rav-Kav card.

**Validating the travel of members of the Security Forces** – the previous audit stated that members of the security forces are not required to validate their travel on public transport and therefore there is no information as to the extent of those travels. The follow-up audit found that rules have been determined for validating travels of the IDF and the Israel Police; as for the Israel Prison Service, such rules have not yet been set. The follow-up audit indicated that the deficiency regarding this subject was well rectified.





## Key recommendations



The Ministry of Transport should act to receive segmented information on concessionaires activity service stations, to examine the trends of service station usage, and act accordingly to improve the service in compliance with objectives. Moreover, the Ministry of Transport should examine whether there is need for additional service centers, particularly for populations with mobility difficulties and for populations having trouble using existing technological means.



It is recommended that the Ministry of Transport complete the regulation of using Rav-Kav cards on public transport, taking into consideration the changes that have occurred in regard to payment and validation for travel on public transport since the last submission of the last bill in 2016, such as applications that have been entered into service for payment and validation for travel on public transport. Regulation is important because the applications serve as additional means of payment and validation for travel on public transportation, in addition to the existing Rav-Kav cards.



The Ministry of Transport, the Ministry of Justice and the Ministry of Finance should complete the regulation of the supervision and enforcement authority on public transport, Particularly in view of the situation where all public transportation users are entitled to enter the vehicle from all doors. The data presented in the proposed amendment to the Traffic Ordinance published in October 2018, whereby 5% to 23% of public transport users avoid payment for travel and do not validate their Rav-Kav cards during the travel, the data regarding the estimated loss to the State Budget following avoiding payment for travel which the Ministry of Finance evaluated at NIS 300 million annually, emphasizes the importance of supervision and enforcement in this regard.



It is recommended that the Ministry of transport complete examination of the monetary compensation setup (the extended tariff) including examining the matter of differentiation for imposing "fines" (the extended tariff) between unpaid travels and paid but unvalidated travels.



The Ministry of Transport should complete the establishment of an external backup site for the Rav-Kav cards setup, due to the various scenarios presented that illustrate the importance of establishing such a site.





### The degree of rectification of the deficiencies stated in the previous audit

Monitoring the use of Rav-Kav cards in public transportation						
Audit Chapter	The audited body	The deficiency in the previous audit	The degree of deficiency rectification as raised in the follow-up audit			
			Not rectified	slightly rectified	considerably rectified	Fully rectified
Issuing Rav-Kav cards	The Ministry of Transport	Large number of service stations is vital to provide quality service to passengers. The issue of Rav-Kav cards is performed at 118 staffed service stations in Israel.				
Recharging Rav-Kav cards	The Ministry of Transport	There is no uniformity in the monthly subscription for trains (30 days from activating the card) and in buses (according to a calendar month).				
		The number of Rav-Kav card recharges via the Internet is low, and there are no recharge stations spreaded out along the major travel routes or in the large shopping				





Monitoring the use of Rav-Kav cards in public transportation						
Audit Chapter	The audited body	The deficiency in the previous audit	The degree of deficiency rectification as raised in the follow-up audit			
			Not rectified	slightly rectified	considerably rectified	Fully rectified
		centers. Most card holders recharge on the bus, with the help of the driver, and the duration stay of the bus at the station is prolonged.				
Recovery of Rav-Kav cards and receiving refunds	The Ministry of Transport	All operators require entitlement examinations for refunds or monetary credits. Whereas the data systems of some operators do not have live data streaming, there is no complete compatibility between the various databases. Therefore a card owner entitled to a refund or requiring recovery of his card must sometime wait 72 hours from the time of applying to the				







Monitoring the use of Rav-Kav cards in public transportation						
Audit Chapter	The audited body	The deficiency in the previous audit	The degree of deficiency rectification as raised in the follow-up audit			
			Not rectified	slightly rectified	considerably rectified	Fully rectified
		service station until it is possible to recover all actions.				
Validation and charging of Rav-kav cards	The Ministry of Transport	Not all Rav-Kav card holders are aware of the fact that they are obliged to validate the tickets even on unpaid travels, for example travels using monthly subscriptions, and they might pay an extended tariff ("fine") as a result.				
	The Ministry of Transport	Expanding the use of open systems (Rav-Kav validation systems that are not adjacent to or require involvement of the driver) requires appropriate enforcement mechanisms to ensure card validation as required				







Monitoring the use of Rav-Kav cards in public transportation						
Audit Chapter	The audited body	The deficiency in the previous audit	The degree of deficiency rectification as raised in the follow-up audit			
			Not rectified	slightly rectified	considerably rectified	Fully rectified
	The Ministry of Transport	and the existence of completed reports regarding passengers numbers.  Members of the security forces are not required to validate their travels on public transportation, and therefore there is no data as to the extent of their travels. Complete information on the number of passengers may assist public transportation operators in planning service routes and schedules and insetting the required payment.				








Monitoring the use of Rav-Kav cards in public transportation						
Audit Chapter	The audited body	The deficiency in the previous audit	The degree of deficiency rectification as raised in the follow-up audit			
			Not rectified	slightly rectified	considerably rectified	Fully rectified
	The Ministry of Transport	The Ministry of Transport should examine the possibility of determining various extended tariffs, and should consider differentiating between an unpaid travel and a paid but not validated travel.				
The service center backup	The Ministry of Transport	There is not backup site for the Rav-Kav cards setup, only for the data, which increases the risk of affecting the service provided to passengers and the revenues following an attack or fault at the service center.				





Monitoring the use of Rav-Kav cards in public transportation						
Audit Chapter	The audited body	The deficiency in the previous audit	The degree of deficiency rectification as raised in the follow-up audit			
			Not rectified	slightly rectified	considerably rectified	Fully rectified
Legislative regulation	The Ministry of Transport	The legislative procedure to regulate the use of Rav-Kav cards has been ongoing for many years. The Ministry of Transport should examine how to promote the legislative procedure.				
	The Ministry of Transport	The issue of protecting Rav-Kav users privacy has not yet been regulated by specific laws, therefore the Law, Technology and Data Authority at the Ministry of Justice (now the Privacy Protection Authority) guidelines for the interim period have been valid for five years and still valid.				





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## Summary

The congestion of traffic on the roads in Israel required promoting public transportation. Over recent years the Ministry of Transport is developing and improving the array of public transportation services throughout Israel. At the follow-up audit completion date, most of the payments for travels on public transportation are performed using Rav-Kav cards, which are reusable rechargeable electronic cards. From mid-December 2020 payment applications and validations for traveling in public transportation were entered into service.

In the previous audit deficiencies were raised regarding issuing and recharging of Rav-Kav cards, Rav-Kav cards recovery and receiving refunds, validation and charging of Rav-Kav cards, engagement for operating a service center and backing up the center data.

The follow-up audit found that the Ministry of Transport rectified around half of the deficiencies stated by the State Comptroller's Office in the previous audit, including adding charging cards stations, adding technological means for charging and regulating the use of cards by IDF soldiers and the Israel Police. However, some of the deficiencies mentioned in the previous audit have not been rectified. For example, the matter of protecting the privacy of Rav-Kav users has not yet been regulated, as well as the supervision and enforcement authority of inspectors.

The importance of promoting public transportation and the need for adapting the means of using it to the current technological changes require that the Ministry of Transport continue its activities to continuously improve the payment means for using public transportation, both Rav-Kav cards and new electronic applications. This should be done together with establishing supervision and control procedures by the Ministry over the way the information on users is stored in the various databases to ensure the protection of privacy of Rav-Kav cards users.





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## Chapter 3

# **State Institutions, Government Companies and Corporations**









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Bank of Israel

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# **Foreign Currency Balances Management by the Bank of Israel – Extended Follow-up Audit**







## Foreign Currency Balances Management by the Bank of Israel – Extended Follow- up Audit

### Background

In October 2012, the State Comptroller published a report on the subject "Management of Foreign Currency Reserves – Bank of Israel" (the previous report)<sup>1</sup>. The report dealt with a variety of issues related to the management of foreign currency reserves (foreign currency reserves or the reserves) held and managed by the Bank of Israel. In view of the inherent importance in holding the reserves, which serve, among others, to contend with economic, financial and political crisis, and due to the changes that occurred in the level of the reserves and their management from the date of publishing the previous report, the State Comptroller's Office performed a follow up audit on the rectification of the deficiencies raised in the previous report as well as several additional issues.

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1 The State Comptroller, **Annual Report 63a** (2012), "Management of Foreign Currency Reserves – Bank of Israel"





### Key figures

**USD 110  
billion**

The desired maximum level of foreign currency reserves as ratified by the Bank of Israel Governor in June 2020.

**USD 185.1  
billion**

The level of foreign currency reserves actually held by the Bank of Israel as of February 2021 (68% over the desired maximum level).

**NIS 555.2  
billion**

The Bank of Israel liabilities in local currency as of end December 2020.

**NIS 70.3  
billion**

The Bank of Israel deficit as of end December 2020.

**USD 7.5  
billion**

The extent of using reserves during the Covid-19 pandemic to contract swap transactions for repayment at local banks.

**58%**

The growth rate in foreign currency reserves levels for 2013 to 2020 due to purchase of foreign currency by the Bank of Israel.

**1.94%**

The rate of surplus yield from actively managing reserves relative to the basis indicator for 2013 to 2020.

**36%**

The rate of risk assets in the reserves portfolio for 2020. The composition – 15% shares, 7% corporate bonds and 14% spread assets<sup>2</sup>.

## Audit actions







From October 2020 to February 2021, the State Comptroller's Office examined the actions taken by the Bank of Israel to rectify fundamental deficiencies raised in the previous report, the changes that occurred in the reserve levels, their management, and the use thereof in times of crisis in general and the Covid-19 pandemic in particular. The audit focused on the Markets Division at the Bank of Israel. Various decisions by the Monetary Committee were also examined.

- <sup>2</sup> Assets carrying higher yield for redemption than that of government bonds with a similar repayment period, due to differences in exposure to credit risk, liquidity, operating factors etc. The yield margin of an asset is the difference between its yield for redemption and the yield for redemption of similar government bonds.



## Key findings


-  **The desired level of foreign currency reserves in international comparison** – the level of reserves at the Bank of Israel (which is 46% of the product as of February 2021) is higher than the desired level according to all customary estimating approaches (which stand at an average of 15% to 22% of the product), and higher than the average level of reserves at comparative countries on all customary indexes. It should be noted that the average level of reserves at comparative countries is also higher than the desired level and indicates a tendency of holding onto a high reserves level.
-  **The level of foreign currency reserves at the Bank of Israel** – as of February 2021 the total foreign currency reserves held by the Bank of Israel were estimated at USD 185.1 billion, whereas the desired level is USD 70 to USD 110 billion. Therefore there is a fundamental deviation of the actual reserves level from the upper bar of the desired level set by the Bank of Israel Governor (on a scale of 68% as of the end of February 2021). This deviation indicate the holding of surplus reserves and may impose risk on the Bank of Israel reputation.
-  **The accumulated deficit in the Bank's capital** – holding a foreign currency reserves portfolio of NIS 557 billion created over the years liabilities totaling NIS 555 billion, most of which are attributed to the accumulation of reserves, and reduced the Bank capital to an accrued capital deficit of NIS 70 billion as of December 2020. The audit found that other than the Bank of Israel, two additional central banks of the nine comprising the comparative group to the State of Israel (Czech Republic and Thailand) have negative capital<sup>3</sup>. Although the transfer of gains is not an objective or duty of the Bank listed by law, the continued deficit in the Bank capital since 1999 (when it transferred NIS 9 billion to the government following a profit registered in 1998) has prevented the transfer of profits to the government, which may have assisted in financing the government expenses.
-  **The use of reserves to achieve monetary policy goals** – it is evident that the foreign currency purchases are compatible to the fluctuations in the NIS to USD exchange rate. However, the purchase of reserves over recent years did not lead to upholding the inflation goal, particularly for most of the period since June 2014, but contributed to devaluation in the NIS value. It should be noted that in light of the deflationary pressures the economy has been contending with over recent years it is possible that without the intervention of the Bank of Israel on the foreign currency


<sup>3</sup> From the financial statements for 2018–2020 published by the central banks. It should be noted that the accounting standards according to which the banks financial statements were drawn up are not uniform.








market the NIS revaluation and the deviation from the inflation goal may have been even higher.

 **Updating the "Procedure for performing financial transactions and investments by the Bank employees to prevent conflict of interest"** – the procedure was last updated on 18.8.15, despite increasing the risk profile and expanding the types of assets in which the reserves portfolio is invested over recent years.

 **A survey of risks at the Bank of Israel** – although according to the markets Division report it is regularly acting to update the various risks, it was found that no risks survey was carried out at the Bank of Israel since August 2013. Despite the substantial changes that have occurred in the reserves level, in their management, in types of assets managed, in the bank systems and in the engagements that the Markets Division performs with external portfolio managers.

 **Evaluating the quality of active management** – the comparison between the yields of active management<sup>4</sup> and the basic indicator, presented to the public in the annual report published by the Bank of Israel, does not allow an optimal evaluation of the quality of the reserves portfolio management. This is because the basic indicator represents a risk free portfolio and as such is with lower yield expectancy than the assets approved for investment as determined by an assets allocation process. In addition, the use of the Information Ration (IR) index alone (which examines the surplus yield of the portfolio relative to its standard deviation), to examine the yield adjusted to risk, does not provide an optimal picture and is not informative when the portfolio yield is negative, as occurred in 2018.

 **Presenting Portfolio management – internally and externally** – over the years, following the increase in portfolio extent and expansion of the investment to riskier assets designed to maximize yields, the use of external management was extended. As of the audit completion date, nine external managers were managing assets comprising 21% of the portfolio, constituting USD 39 billion, of which: shares forming 15% of the portfolio, MBS (mortgage-backed securities)<sup>5</sup> in the USA forming 2% of the portfolio and corporate bonds on the European and USA markets forming 2% of the reserves on each market. At the same time, the Bank of Israel annual statement does not present the assets managed by external management separately.

 **The use of reserves during the Covid-19 pandemic** – the audit did not find indications during the Covid-19 pandemic, and particularly in March 2020, the Bank of Israel was examining sale of foreign currency, at a time that the USD exchange rate reached a peak of NIS 3.862 per USD 1. It should be noted that during 2020 the reserves

<sup>4</sup> Active management refers according to the Bank of Israel definition to decisions to invest in assets and in countries that are not included in the basic indicator.

<sup>5</sup> A security with a future flow backed by a fund and interest payments on a mortgage collection.



level at the Bank of Israel increased relatively to all countries comparable to the State of Israel in both billions of USD and in change rates (a difference of USD 29.8 billion from the average change in comparable countries and a difference of 24.5% in the average change rate in these countries).



**Rectifying deficiencies raised in the previous audit** – most of the deficiencies noted in the previous report, including the lack of procedures regulating the activity, including formulating guidelines for investment, differentiating between rules of compliance, the investment, numeraire calculation procedure<sup>6</sup> and a data and cyber security procedure – were including rectified, alongside handling the portfolio risks in general extreme cases (as detailed in the follow up audit findings table).

**Activity of the Markets Division at the Bank of Israel** – given that the continued and substantial deviation in the foreign currency reserves from the desired level, the State Comptroller's Office commends the markets Division work to update the investment goals, composition of the currency indicator, method of measuring the reserves holding yield and updating the risk profile of the portfolio.

## Key recommendations



It is recommended that the Bank of Israel continue to examine the desired reserves level in a timely manner and the extent of deviation thereof, and present reasons for accumulating surplus reserves and the costs inherent therein. Moreover, it is recommended to continue examining extension of the deviation from the desired reserves level, and if necessary to take action for its resolution.







It is recommended that in view of the deviation from the desired level of reserves, the Bank of Israel examine the need for change in the principles according to which the governor will determine the desired level of long-term foreign currency reserves, with approval of the Minister of Finance. It is also recommended that as financial advisor to the government, the governor continue to advise the government about formulating export incentive policies for the Ministry of Finance, as an alternative to purchasing reserves. These actions should be taken alongside continued examination of the use of other monetary tools to support achievement of the monetary policy objectives, paying attention to the cost created by deviating from the desired level of reserves and the risks entailed therein and the effectiveness of purchasing foreign currency to fulfill inflationary goals.

<sup>6</sup> A currency basket determined by the monetary committee derived from possible uses of reserves in times of need and from investment goals that reflect the holding objectives.





-  It is recommended that alongside the Bank of Israel's activity on the foreign currency market (paying attention to the Bank of Israel research findings of 2017 detailed in the report concerning the effectiveness of the bank's intervention on the exchange rate for supporting exports) the Ministry of Finance examine the use of fiscal tools to promote export according to government policy.
-  It is recommended to prepare a contingency plan, for examination by the Monetary Committee, to realize surplus reserves effectively in suitable circumstances to reach the desired level and reduce the risk imposed on the Bank of Israel's reputation.
-  It is recommended that the Bank of Israel perform an updated risks survey, particularly concerning the Markets Division activities, which will suit the frequent changes in the reserves portfolio. These changes may cause direct monetary damage and even generate realization of risks. It is further recommended to ensure that a comprehensive risks survey is conducted at least once every four years as determined by the Policy Document of 2013.
-  In order to increase transparency in the portfolio management in view of the increasing exposure to fluctuating assets, it is recommended to present to the public, as part of the annual report, the external management performance, which has inherently greater risks in terms of yield adjusted to risk, and particularly for assets managed also internally. In addition, it is recommended to examine presentation of the portfolio yields relating to additional indicators used by the Bank of Israel in managing the portfolio, including the committee indicator<sup>7</sup> and the tactical indicator<sup>8</sup>, and examine the possibility of using additional indexes to estimate the yield adjusted to risk and its consistency over time. Adding indexes will assist in receiving a broader and more reliable picture, as done by the division in 2015 and 2016.

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7 Reflecting the strategic component of the assets in the portfolio, as chosen by the Monetary Committee.

8 Added to the strategic component of the assets in the portfolio and including the exposures of the markets division at strategic level within the degrees of freedom it was awarded.





### Key findings of the follow up audit

Audit Chapter	The deficiency in the previous audit	The degree of deficiency rectification as raised in the follow-up audit			
		Not rectified	slightly rectified	considerably rectified	Fully rectified
Change in Principles for Setting the Proper Level of Foreign Currency Reserves	Principles for setting the proper level were established, but no decision was made as to which changes in principles require the approval of the Finance Minister, as required by law.				
Regulation of Investment Activity	The guidelines for investment policy, methods of risk management, principles for measurement of returns, and levels of flexibility in investment are scattered throughout various systems and documents and not gathered in a single updatable document.				
Directive for Calculation of 'Numeraire'	Even though there have been changes in the procedures for setting the 'numeraire', the Market Division's Directive for its calculation was last updated only in October 2006, and therefore is in effect irrelevant.				





Audit Chapter	The deficiency in the previous audit	The degree of deficiency rectification as raised in the follow-up audit			
		Not rectified	slightly rectified	considerably rectified	Fully rectified
Risk Profile for Reserves Portfolio	No tool was found which could aid the Market Division in analyzing the overall risk to the reserves portfolio in times of extreme circumstances.				
Distinction Between Rules for Investment and Rules for Compliance	No clear distinction was made between the rules for investment and the rules for compliance, and there was no regulation setting the jurisdiction for approval of action reports and the method for dealing with deviations from the rules.				
Procedure for Cyber and Information Protection	There was no procedure set in place for categorization of sensitive documents, which would regulate the methods of documentation, protection, distribution, persons permitted to view said documents, and methods to update and track the various copies existent of said documents.				





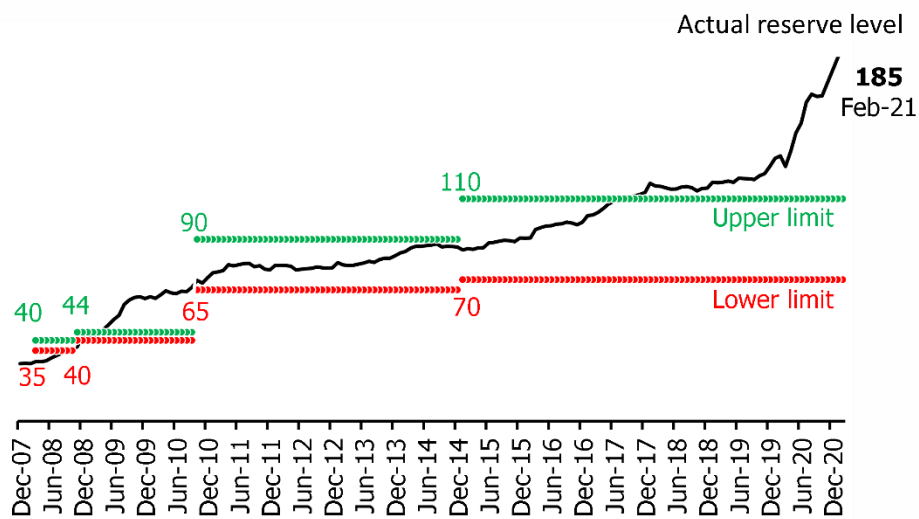
Audit Chapter	The deficiency in the previous audit	The degree of deficiency rectification as raised in the follow-up audit			
		Not rectified	slightly rectified	considerably rectified	Fully rectified
Oversight of Connecting Transactions	The commercial system of the Bank does not support the procedure for connecting transactions, which requires connecting two investment managers in transactions over a specific sum.				
Procedure for Receipt of Bids	The Division does not perform total oversight regarding the procedure for receipt of bids by employees in the transactions room, and therefore there is no oversight regarding the operational risk of an employee not receiving a number of bids or not choosing the best one.				







**Actual reserve level compared to desired level as determined by the Bank of Israel governors, December 2007 to February 2021, in billions of dollars**

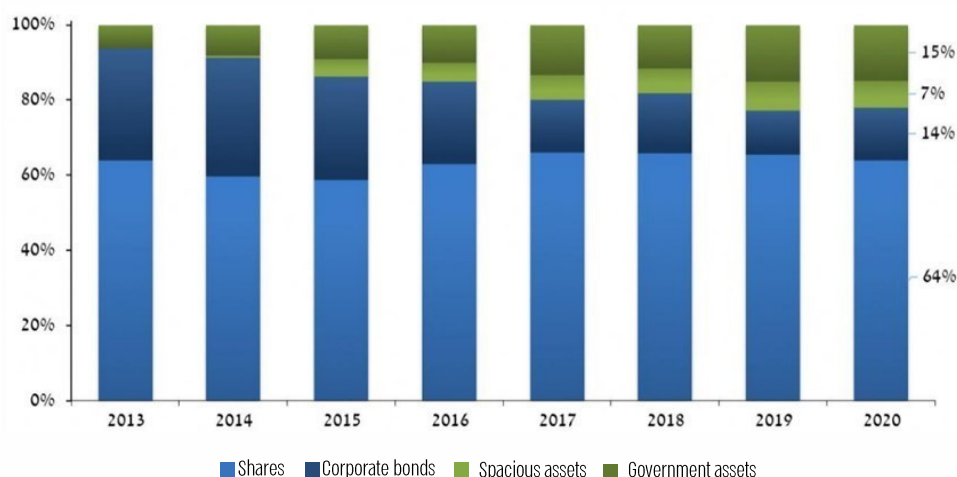


Bank of Israel data processed by the State Comptroller's Office.





### Composition of the reserve portfolio according to assets, 2013 to 2020, in percentage



The source: Bank of Israel.

## Summary

The follow up audit on the subject of managing foreign currency reserves at the Bank of Israel indicated that over the past decade, following the implementation of the Bank of Israel Law 2010, the activity of the Bank of Israel on the foreign currency market have been regularized. Inasmuch, the need for change in the principles on which the desired level of long-term foreign currency reserves is frequently examined, as are the guidelines for investment policy therein. In addition, most of the deficiencies found in the previous report published in October 2012 have been rectified, including the lack of procedures to regular the Bank of Israel activity and to handle risks in the reserves portfolio in general and in radical events in particular. At the same time, a significant increase over the past decade in the rate of foreign currency reserves held by the Bank of Israel (in light of global financial developments), caused, in February 2021, a deviation of USD 75 billion from the top echelon of the desired rate set by the governor, increased the investment risks and created extensive liabilities in the bank reserve to the scope of NIS 555 billion, most of which are related to accrued reserves, alongside reduced bank capital to an accumulated capital deficit of approximately NIS 70 billion, as of December 2020. In order to return to the desired investment rate in the foreign currency reserves and to reduce the foreseen risk to the bank's reputation, a contingency plan





should be prepared to be examined by the monetary committee, to realize surplus reserves effectively in suitable circumstances.





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Yad Vashem

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# **Aspects in the Activities of Yad Vashem – The World Holocaust Remembrance Center**







## Aspects in the Activities of Yad Vashem – The World Holocaust Remembrance Center

### Background

Yad Vashem – The Holocaust and Heroism Memorial Authority (Yad Vashem) is a public corporation operating by power of the Martyrs' and Heroes Remembrance-Yad Vashem Law 1953. According to this law, the role of Yad Vashem, among others, is to gather into the homeland material regarding all those members of the Jewish people who laid down their lives, who fought and rebelled against the Nazi enemy and his collaborators and to perpetuate their memory and that of the communities, the organizations and the institutions which were destroyed because they were Jewish and to commemorate the memory of the righteous among the nations. The Yad Vashem campus is spread over 180 dunams on the Memorial Mount in Jerusalem, and includes museums holding items and documents related to the holocaust, research and education centers, memorial monuments and sites, such as the Hall of Remembrance, the Valley of the Communities and the Children's memorial. In order to contend with the challenges of commemorating the holocaust today, 75 years after the ending of World War II, Yad Vashem has created a multi-dimensional memorial and learning environment comprised of four major components: documentation, research, education and commemoration. Yad Vashem serves as the public trustee for achieving the objectives determined in the Yad Vashem Law. Yad Vashem is a part of the civil service, and is subject to liabilities imposed by Civil Law.





### Key figures

**NIS 200  
million**

The ongoing annual budget (not including the development budget) of Yad Vashem for 2017–2019.

**NIS 25.6  
million**

The Yad Vashem deficit from ongoing activities for 2020 (Covid-19 year).

**NIS 81  
million**

The accumulated annual deficit from ongoing activities for 2020 to 2024 according to the Yad Vashem forecast as presented to the Yad Vashem financial committee in March 2020.

**NIS 101  
million**

The total donations raised by Yad Vashem in 2019. This amount is 52% of the total Yad Vashem revenues in that year.

**1%**

Of donors donated approximately 79% of the Yad Vashem donations in 2016–2019.

**1.1  
million**

People visited Yad Vashem in 2019. Due to Covid-19 restrictions, in 2020 Yad Vashem was visited by 195,000 visitors.

**Approximately  
10,500  
items**

Require urgent preservation. Approximately 1,200 art works on paper, and 6,500 paper objects and 3,000 textile items are high in priority for preservation.

**In more  
than 80%**

Of the measurements taken by the State Comptroller's Office in the archives that contain paper items, deviations were found in the humidity levels.

## Audit actions



From July 2019 to November 2020 the State Comptroller's Office examined several issues pertaining to core activities of Yad Vashem: the museum operations including items registration, storage and preservation of collection items and their presentation on the Yad Vashem Internet website; holocaust research activity; donations collection activities; aspects concerning the activity of administrative institutions, and the current budgetary balance of Yad Vashem.



## Key findings



**Preventive preservation** – the Museum Regulations 1984, and the Archives Regulations (Conditions for Approving Public Archives and the Regulations for their Management) 1957, determine that the museum must take "preventive preservation" actions. Preventive preservation includes a variety of actions that do not involve handling the items themselves, and which are designed to limit the factors damaging the items by controlling environmental conditions, particularly temperature, humidity and light. Following are the audit findings regarding this matter:

- **Lighting and radiation** – Yad Vashem uses fluorescent lighting which produces ultra-violet radiation. Not in accordance with the preservation conditions determined for museum spaces whereby it is preferable to block the radiation completely, in ten storage spaces the fluorescent lights were not covered. In Addition, in three exhibition halls the lighting level measured was higher than that determined by the Museums Department directives.
- **The humidity** – over 80% of the measurements performed in years 2016–2019 in the archives that contain paper items showed deviation from the desired humidity levels, by up to 59%. Moreover, 6.6% of the measurements performed in this period in the pictures warehouse showed deviations from the permitted humidity, reaching almost 140%.
- **The temperature** – from 2016 to 2019 deviations were found in the temperature of the pictures warehouse in 4.9% of the measurements, deviation that reached 396%. It was further found that for this period in 66% to 73% of the temperature measurements in the archives that contain paper there was a deviation from permitted temperatures that reached 20% to 30% in the various warehouses.

The audit also found that in the storage spaces there is no warning system for flooding.

It should be noted that Yad Vashem has begun to establish the "collections hall" in which the items will be stored in conditions that will enable preventive preservation.



**Fundraising** – from 2016–2019 around 1% of yad vashem donors contributed 79% of the donations amount (111 million dollars of the total 140 million dollars). In those years 26% to 39% of the donations received by Yad Vashem were from only a few donors – that is, approximately one-sixth of the Yad Vashem budget is dependent on few donors. Receiving large donations from a small number of donors enhances the dependence of Yad vashem on fundraising. The dependency on fundraising increases the risk to the ability of Yad vashem to continue its activity in times of crisis, such as the Covid-19





pandemic, and may bring about a decrease in the amount of funds raised, particularly for ongoing activity. Most of the funds raised by Yad Vashem through direct approaches to donors, and in 2019, during the audit period, Yad Vashem began conducting a strategic work to examine the possibility of fundraising via the Internet, social media, crowd funding, etc. This strategic work has not yet been completed.



**Fundraising from potential bequests and engagements with fundraisers** – Yad Vashem has no written procedure that includes reference to issues of the unjust influence on potential bequests according to distinctions determined by law. Moreover, Yad Vashem did not hold a tender before engaging with two suppliers for fundraising, and no protocols of the Tenders Committee or any other documents stating that the contract with the two service providers and their extensions are exempt from tenders, were found. It should be stated that the contract amount with the two fundraisers totals NIS 1.9 million annually.



**The current budgetary balance of Yad Vashem** – according to the Yad Vashem financial statements for 2020, the annual deficit from current activities was NIS 25.6 million and the amount of donations for current activity decreased from NIS 101 million in 2019 to approximately NIS 80 million in 2020. 2020 was an irregular year due to the Covid-19 pandemic, however the five year forecast prepared by Yad Vashem in 2019 and presented to the Finance Committee in March 2020, already expected current annual deficit in 2020 of approximately NIS 10 million. According to the five-year forecast, the accumulated annual deficit from current activities for 2020–2024 would be approximately NIS 81 million. At the audit completion date, the Yad Vashem management has not yet completed a program for reducing the current annual deficit forecasted in the plan for 2020–2024. However, it should be stated that according to the financial statements for 2020, Yad Vashem has a net assets balance on which there is no limitation designated by the management for a total of NIS 97 million.



**The Administrative Institutions** – over recent years developments and changes have taken place regarding the adoption of corporate governing rules, an issue that was expressed in the criteria determined by the Council for Public Corporations. The Yad Vashem articles of association determined the establishment of three administrative institutions, but did not clearly define which entity was designed to outline policy and supervise the management's activity, and the roles of CEO and subordinates managers were not defined, as proposed by the Council for Public Corporations. The audit also found that in November 2020, 93 members served in the public council; the appointment validity for 83 of them had expired, as they were not extended by the appointing Ministers and bodies. In addition, it was found that in November 2020 the number of women among the council members was less than a third.





**Establishing the collections hall** – at the time of the audit Yad Vashem was in the process of establishing a collections hall – a building designed in the 1990's and is designated for storing collection items under optimal preservation conditions. In August 2020 the building permit was received; occupancy is scheduled for December 2022.

**Ensuring accessibility of holocaust remembrance through digital means** – the State Comptroller's Office commends the Yad Vashem activity to promote the accessibility of the Yad Vashem website.

## Key recommendations

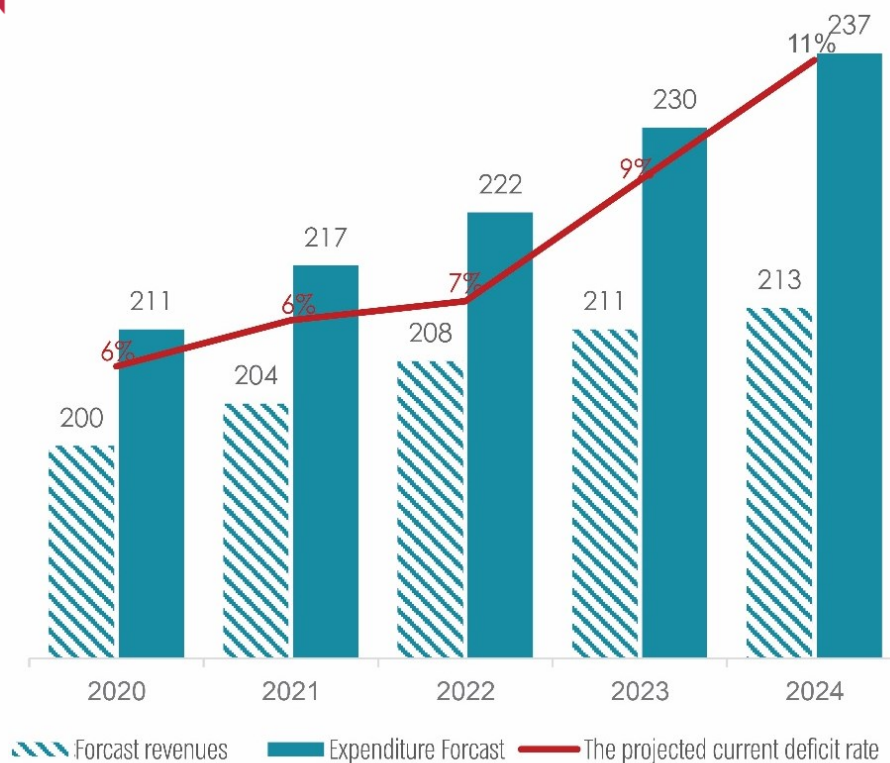
- 💡 It is recommended that Yad Vashem examine the items requiring preservation and document the necessary information in the Sapir system, in order to prepare a work plan for preserving the items. It is also recommended to prepare a preservation plan for items whose condition requires immediate handling.
- 💡 It is recommended that Yad Vashem take the necessary actions to reduce possible damage to items, periodically including performing frequently testing including testing the level of light, radiation, temperature and humidity in the museum halls and warehouses. It is also recommended that Yad Vashem verify that its procedures provide full solution to the need for monitoring and control to prevent possible damage to exhibits, and that the procedures include reference to the handling of deviations.
- 💡 It is recommended that Yad Vashem management formulate a fundraising policy based on a multi-year vision, including matters pertaining to the percentage of donations used as a source for the Yad Vashem ongoing activity. It is further recommended that the Yad Vashem management complete its strategic work for examining innovative ways for digital fundraising. In all matters pertaining to contracts with fundraisers, Yad Vashem must act according to the Tenders Committee procedure. The State Comptroller's Office state that the high road to these engagements is the issuing of a public tender. If Yad Vashem believes that the contracts with the two fundraisers are exempt of a tender, it should bring this issue up for a discussion of the Tenders Committee to determine whether to grant such exemption.
- 💡 It is recommended that Yad Vashem complete the formulation of an updated and balanced plan for 2021–2024. This need is emphasized by the Covid-19 crisis and its effect on the Yad Vashem activity during 2020–2021.
- 💡 The State Comptroller's Office recommends that Yad Vashem and the Ministry of Education, together with the Ministry of Justice, examine whether changes are required in the articles of association and the legal structure of Yad Vashem; examine settling the necessary checks and balances at Yad Vashem between the supervising and executing





bodies; examine adopting the recommendations of the Council for Public Corporations and the principles determined in the bill of the Public Corporations Law 2013; consider amending the regulations so that the role of Yad Vashem CEO, his authority and responsibility are determined, as well as the role, authority and responsibility of the board of directors; and outline a policy for supervising the work of the CEO. In addition, the Minister of Education and all the recommending bodies should complete the appointment of the missing council members on their behalf and decide concerning renewing the appointment of council members whose appointments have expired. In the process of completing staffing and appointments it is recommended to maintain appropriate gender representation and representation of various sectors of Israeli society.

### The revenues and expenses forecast of Yad Vashem for 2020–2024 (in millions of NIS)



According to Yad Vashem data as presented to the Yad Vashem finance committee in March 2020, as processed by the State Comptroller's Office.





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## Summary

Yad Vashem holds large collections of objects and documents of unique historical value designed to assist in commemorating the holocaust. The audit findings show the need for improving the management of these collections, to ensure their preservation for the generations to come. As part of this process, Yad Vashem should improve its recording and cataloging of the items; should computerize the preservation activities and operate to complete them before the condition of the items deteriorates; should verify adhering to standards of temperature, humidity and lighting in compatibility with updated museums standards. Yad Vashem should review the annual deficit derives from current activity, and therefore the Yad Vashem management is required to take action to annually balance the budget.









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Israel postal Company Ltd.

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# **Financial Aspects of the Israel Postal Company Activity**







## Financial Aspects of the Israel Postal Company Activity

### Background

The Israel Postal Company Ltd. (the Postal Company or the Company) is a government company fully owned by the State, which began operating in March 2006 according to a license awarded by virtue of the Postal Law 1986 directives. The Company is subject to supervision of the Government Companies Authority (the Companies Authority) and in certain areas of its activity it is also subject to supervision by the Ministry of Communications. Over the past years the Company has been contending with financial difficulties. A multi-year examination and analysis of the Company's financial statements, including analysis of its major financial ratios, provides an indication regarding the Company's financial situation, the trends and risks of its activity, the difficulties it has to contend with, the means and actions it takes to deal with them and the profitability of every activity sector. As part of this audit a multi-year review of the data included in the Company's financial statements was conducted.





## Key figures

**NIS 229  
million**

The deficit in the Company's working capital at the end of 2019. At the end of 2020 the deficit in the working capital totaled NIS 519 million.

**4.95%  
rate**

The Company's gross profit at the end of 2019. In 2017 this rate totaled 8.06%.

**45% rate**

The reduction, between 2013–2020, in the quantity of traditional postal deliveries.

**200%**

The growth rate, between 2012 and 2019 in the scope of imported deliveries from international online trading.

**NIS 1.13  
billion**

The Company's salary expenses for 2019.

**NIS 578  
million**

The total liabilities the Company made to its employees for budgetary pension, as of 31.12.19.

**240 assets**

Has not yet been fully Registered under the Company's name, as of 31.12.19.

**8.65%**

The annual weighted interest rate above prime charged by the Postal Bank for payment plans.

## Audit actions



From May to December 2020 the State Comptroller's Office examined various financial aspects of the Postal Company's activity. Among others, the emerging trends and risks were examined in view of the financial statements findings, development of the Company's growth engines and the operating and financial data systems on which, among others, the statement information, was based. This audit also examined the regulatory and control of the Company by the Government Companies Authority and the Ministry of Communications in this area. The audit was conducted in the Postal Company and its subsidiary, the Postal Bank Company Ltd. (Postal Bank). Supplementary examinations were conducted at the Government Companies Authority and the Ministry of communications.



## Key findings



**Deficit in working capital** – The Company had a working capital deficit of NIS 229 million as of 31/12/19, a 44% increase compared to its rate as of 31.12.18. At the end of 2020 there was an additional worsening in the working capital deficit parameter – the deficit totaled approximately NIS 519 million.



**The gross and operational profit rate** – During 2017–2019 there seemed to be a trend of reduction in the Company's gross profit rate from 8.06% to 4.95%, pointing to a continuous erosion in the financial outcomes of the Company's business activity for the examined years. The Company's operating profit rate for 2019 totaled 2.53% and was approximately 20% lower than the common rate in postal companies worldwide.



**Cash flow** – At the end of 2019 the Company had a positive cash flow from an ongoing activity totaling NIS 46.2 million compared to NIS 95.5 million at the end of 2017 – a reduction of more than 50%. Continuation of this situation will affect the Company's ability to maintain appropriate ongoing operating capacity and to perform new investments without addressing external financing sources.



**Reporting by sectors** – Reporting by sectors show that the profitability of the company decreased in all sectors of its activity in 2019. In the post and retail sectors its annual losses totaled NIS 69.5 million and its profits from trade and financial services sectors dropped from NIS 67.5 million in 2018 to NIS 37 million in 2019.






**Traditional postal services** – As part of the traditional postal services the number of letters sent via the Company decreased from 521 million letters in 2013 to 286 million letters in 2020, a reduction of 45%. Revenues from this area of activity decreased from NIS 912 million in 2013 to NIS 632 million in 2020, a reduction of 31%.



**Implementing full structural separation between the Postal Company and the Postal Bank Company (amendment 11 to the Postal Law)** – Amendment 11 from 2012 has not yet been implemented, no structural separation between the Postal Company and the Postal Bank has been performed and the areas of the Postal Bank activity have not been extended. This affects the development potential of the Postal Bank and its potential for revenues, and perpetuates the mixture of the tangible with the financial assets. In addition, it should be noted that in the opinion of the financial statements of 2019 the external CPA expressed reservations concerning the fact that the Postal Bank Company, attributed all its revenues to the Israel Postal Company Ltd (the mother company).








-  **Company salary expenses** – Despite the execution of the Company's retirement plan, which was financed by the State at NIS 477 million, including reduction of the total number of positions to 5,050, the salary expenses of the Company showed an increase in the four years between 2016–2019 (the agreement with the State was signed in 2015) from NIS 1.08 billion in 2016 to NIS 1.13 billion in 2019, thereby affecting the Company's profitability.
-  **Registration of Company assets** – According to the Company's financial statement for 2019, the registration in the Land Register of 240 (71%) of the Company's 339 assets has not yet been completed, and the legal registration process has been fully completed for only 99 (29%) of the assets. The incomplete registration of 71% of the Company's real estate assets under the Company's name may affect its rights.
-  **Preparing for the privatization of the Company** – At the audit completion date (December 2020), six years after the government decision on the matter was made, the Companies Authority has not yet commenced a financial examination to estimate the Company's value, and privatization of the Company has not yet been completed.



**Reporting by sectors** – The Company commenced reporting by sectors of activity in its statements for 2019.

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## Key recommendations

-  **Improvement in Company liquidity** – The Company should act to improve its liquidity and to close the working capital deficit. It is further recommended that the Company act to improve its activity in all sectors and to locate growth engines for its operations in order to maximize profits from its ongoing activities
-  **Examining adjustments in the license terms** – It is recommended that the Ministries of Finance and of Communications complete an examination of the need for adjustments in the license terms and formulate a plan for the Company's future development, taking into account its regulatory obligations, to the need to provide possibilities encourage the company to compete with other companies in order to maintain the Company's financial resilience.
-  **Promoting amendment 11 of the Postal Law** – In view of the effect the Postal Company situation has on the development of the Postal Bank and its capability to provide a solution for disadvantaged populations, thereby promoting competition between the banks in Israel, there is a growing need to adapt the Company's license terms to a competitive market. Upon completion of the process, it is recommended that the Ministries of Finance and of communications monitor the implications and take



measures to implement the separation, in coordination with the Bank of Israel, in order to promote amendment 11 and convert the Postal Bank into a fully licensed bank.



**Drawing Conclusions regarding the salary structure in the Company** – It is recommended that the Company, the Budgets Department and the Salary and Employment Agreements Department in the Ministry of Finance and the Companies Authority draw conclusions regarding the implementation of the rehabilitation agreement signed in 2015 and act to include in the rehabilitation agreement alongside goals for reducing the number of employees and a salary structure that will support the Company's profitability.



**Resolving real estate rights** – It is recommended that the Postal Company, assisted by the Israel Land Authority (ILA) and the Real Estate Registration and Settlement Department in the Ministry of Justice, complete actions to settle its rights in its real estate assets, conclude leasing agreements with the ILA and fully register its rights in the land assets at the Land Registration Bureau, particularly in view of its substantial assets and the expected privatization process.

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## Summary

The current audit report details the fundamental trends and risks emanating from the Company's financial statements, including regulatory risks and fluctuating conditions in the postal market, that may make it difficult for the Company to continue providing its services to the public in the long term. The report indicates a trend of worsening in the monetary and financial results of the Company over the years. The report also indicates the lack of substantial accounting information on various areas of the Company's activity and details additional deficiencies regarding the Company's financial activities.

It is recommended that the Postal Company, the Companies Authority and the Ministries of Finance and of Communications operate to rectify the deficiencies emanating from this report and examine implementation of its recommendations accordingly.









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Mekorot Water Company Ltd.

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# **Mekorot Water Company Ltd. – Financial Audit**







## Mekorot Water Company Ltd. – Financial Audit

### Background

Mekorot Water Company Ltd (the Company or Mekorot) is a government company designed to develop the water resources in Israel and provide water to its residents. The Company is the provider of a vital service and a natural monopoly in the field of water supply. The Company is also a "National Water Authority" and its duties include establishing the national water enterprise (the National Water Carrier), managing it and provide water from it. Government decision 4514 of February 2019<sup>1</sup> determined several steps to reinforce the financial resilience of Mekorot and improve the efficiency of the water economy, among others due to a situation that requires performing significant investments in the water economy. The Government Authority for Water and Sewage (the Water Authority) is in charge of managing the water and sewage economy and among others determines the revenues and the tariff of Mekorot.

1 Decision 4514 by the 34th government "Creating an infrastructure to increase the extent of development in the water economy in order to contend with prolonged periods of drought and amendment of government decisions" (24.2.19)





## Key figures

**20%**

The portion of the Mekorot component in the average water tariff for home consumers in years 2012–2019<sup>2</sup>.

**1,659 MCUM**

Supplied by Mekorot in 2020, which are 69% of the total water supply in Israel and approximately 82% of home consumption.

**NIS 1.5 billion**

The extent of Mekorot investments for each year from 2020–2022 according to the development plan approved by the Water Authority in December 2019.

**5.4%**

The actual rate of return on capital for 2020 (1.6% in 2019). Mekorot's normative yield rate totals 5.5% according to cost rules.

**NIS 13.5**

**billion**

Mekorot's total liabilities as of December 2020. In this component there has been a growth of 24% in years 2016–2020 compared to a growth of 24% in fixed assets and a growth of 16% in equity. This situation weakens the Company's financial resilience.

**NIS 3.9 billion**

Total revenues from water sales for 2020. The total profit for this year reached NIS 199 million (compared to a loss of NIS 24 million in 2019 among others due to the costs of the early retirement program which totaled NIS 264 million, according to the collective agreement of June 2019 regarding Mekorot's efficiency).

<sup>2</sup> Thus, for example, in 2019 Mekorot comprised an average consumer tariff of NIS 1.829 per CM which is 20% of the average residential consumer tariff which totaled NIS 9.02 per CM.



## Audit actions



From August to December 2020 the State Comptroller's office audited financial issues associated with the Mekorot Company's consolidated statements – which include the subsidiaries that are almost fully owned by Mekorot. The subjects examined were: presentation of the consolidated financial statements, analysis of essential sections in the consolidated balance sheet and the profit and loss statement; financial ratios from the consolidated statements; analysis of the disparities between recognized costs in tariff sources and actual costs; analysis of the budget against actual performance; the implementation status of steps determined by government decision 4514 and obstructions to implementation. In addition, data for 2016–2020 was examined. The audit was conducted at Mekorot and the Water Authority. Supplementary examinations were conducted at the Ministry of Finance, the Ministry for Water Resources and the Government Companies Authority.

## Key findings



**Debt coverage ratio** – in 2015–2016 the debt coverage ratio<sup>3</sup> of Mekorot was over 10% and reached 14.6% in 2016. From 2016 a sharp drop occurred in the debt coverage ratio to a rate of 4.5% in 2018, which expresses a decrease in the Company's debt repayment ability through the annual flow from ongoing activities. In 2019 an increase to a rate of 7.2% occurred. According to Mekorot statements from December 2020, the rate of this ratio is 8.6%. It should be stated that the debt coverage ratio of Mekorot is low compared to the average ratio for 2016–2018 of infrastructure companies in Israel and worldwide, where it ranges from 10%–18%.



**The leverage ratio** – since 2017 there has been a consistent increase in the leverage ratio<sup>4</sup>, and it reached a rate of 69% in 2019. According to Mekorot statements from December 2020, this ratio is 70.6%. The higher the leverage ratio, the more the Company relies on external capital for financing its activity and less on its own equity. It should be stated that the leverage ratio of Mekorot is high compared to the average






3 The debt coverage ratio expresses an operational profit (loss) with added depreciation discounts and additional sections that do not entail cash flows and deducted of interest and tax payment, relating to the scale of debt. The index expresses the Company's ability to regularly fulfill repayment of its loans (including bonds).

4 The leverage ratio is calculated as the ratio between the adjusted debt and the equity capital.






leverage ratio for 2016–2018 of infrastructure companies in Israel and worldwide, where the ratio is 60%.


-  **Reporting of activity sectors** – the sectoral reporting in the Mekorot books does not differentiate between activities according to the various types of water as separate profit centers – desalinated water, natural clear water, treated waste water and brackish water – as required by government decision 2318<sup>5</sup>.
-  **Investments in the innovations and improvements budget** – from 2015–2019 the annual companies water utilities depreciation was on average NIS 525 million. The development budget for those same years was on average NIS 843 million, and the innovations and improvements budget was on average NIS 153 million, and matched the maximum investment amount defined in the rules. However, the average innovations and improvements budget was 4 times lower than the average annual depreciation for these years and 3 times the annual depreciation for 2019. The data indicates that most of the Company investments are in new water utilities and not in upgrading or improving existing water utilities, among others, due to the need for establishing new water utilities to expand the supply network and increase the transferable quantity of water, reliability of the water supply and the connection of areas that are not yet connected to the water system.
-  **The actual interest costs compared to recognized interest costs** – the actual interest costs of Mekorot for 2015–2019 were higher than the recognized interest costs in the tariff, due to weighted raising of average 12 years life span bonds which is higher than the average life span recognized in the tariff (ten years). In 2019 the difference was NIS 80 million. This difference and its expansion may affect the Company's upholding of financial resilience objectives.
-  **Collecting water fees from private producers** – by the audit completion date, December 2020, NIS 245 million owed by private producers were not collected, however according to rules of costs by the end of 2020 the Mekorot tariff for 2019 included NIS 115 million recognized as income from water fees, despite Mekorot not having actually collected them. Despite the Ministry of Energy CEO and the Water Authority's Economy Deputy Director General having notified at the Mekorot board of directors meeting in December 2019 of the Water Authority Administration's commitment to the outline of amending recognition in the tariff concerning private producers' debts, by the audit completion date the Water Authority Council had not yet amended the recognition outline as said.
-  **Implementation of the directives determined in Government Decision 4514 of 2019 to reinforce the financial resilience of Mekorot** – by the audit completion date the following steps included in the government decision had not been completed –


5 Government decision 2318, "Structural change in the Mekorot Group" (26.8.07).



transfer of rights in NWC assets<sup>6</sup> and sale of the wastewater utilities and establishment of two other wastewater utilities (the wastewater issue is a condition for transferring NWC assets). Implementing these steps is among the conditions for promoting vital programs to improve Mekorot's financial ratios and its attainment of the goals set by the Financial Resilience Team according to Government Decision 4514, including the plan to register NWC assets in the Mekorot books and the program for betterment and sale of Mekorot lands and assets.

 **The program for betterment and sale of lands and assets** – Mekorot located four real estate assets for sale, of which the board of directors approved two for sale. The sale thereof is expected to improve the debt coverage ratio and leverage ratio. It was found that at the audit completion date, public tenders for the sale of the four real estate properties, which are designated for sale by tender procedure, had not yet been published.

 **Sale of recovery water utilities that Mekorot is required to sell** – due to a dispute between the Water Authority and Mekorot concerning the sales procedure of six wastewater treatment water utilities to private wastewater suppliers, Mekorot has not completed the sale of these water utilities, despite the government decision having determined and it being agreed by Mekorot that the sale would be performed no later than 31.10.19.

 **The financial goals set for Mekorot** – the Financial Resilience Team<sup>7</sup>, acting according to Government Decision 4514, set the following financial goals for Mekorot: (a) debt coverage ratio for 2020 to 2025 of no less than 8%; for 2026 to 2029 no less than 9%; and from 2030 no less than 10%; (b) a maximum leverage ratio that will not exceed 70% of year 2022, and aspiring to achieve 65%. In view of the findings in this report and the obstructions preventing unification of the NWC assets stated in the Mekorot books, there is concern that the Company may not achieve all of the determined goals.



**Mekorot rating** – Mekorot rating for June 20 is AAA\Stable. This rating is high and stable compared to tariffed government infrastructure companies in Israel.

**Improving the efficiency of Mekorot's energy expenses** – From 2015–2019 the Company improved its energy efficiency. In 2015 actual expenses exceeded the tariff

6 The assets of the National Water Carrier (NWC) were defined in Government Decision 2306, "Mekorot - structural change" (30.7.02), as "real estate assets and the attached thereto known together as the National Water Carrier that are designated, used and held to provide water and all the government assets designated and used to provide water and are held by the Mekorot Water Company for the government...".





7 A team headed by the Companies Authority Manager and the Water Authority Manager and participated by representatives from the Budgets Department, the Accountant General and the Ministry of Energy together with Mekorot.





recognized expenses by a total of NIS 3.1 million; in comparison, in 2019 the actual expenses were lower than the normative expenses creating a profit of NIS 26.4 million. Most of the energy efficiency derived from electricity purchasing agreements with private electricity manufacturers and replacing equipment to reduce energy expenses.

## Key recommendations

-  It is recommended that Mekorot, the Water Authority and the Financial Resilience Team operate to prevent deterioration in the Company's debt coverage and continue to act to implement the steps determined in Government Decision 4514 of 2019 to reinforce the Company's financial resilience and thereby prevent any situation where demoting Mekorot's rating may be considered.
-  It is recommended that alongside the promotion of new water utilities in the development program determined by the Water Authority, as part of the development program determination process the Water Authority examine Mekorot's investments in the existing systems compared to their annual depreciation and life span in order to maximize the benefit in preserving existing systems.
-  It is recommended that Mekorot continue to act to complete the realization of the four assets it located and formulate a multi-year plan for asset betterment. This becomes more acute in view of the value differences of the said four assets between their current condition and their condition as available for construction. It is further recommended that Mekorot perform assessor evaluations of additional relevant assets and consider presentation at fair value in the notes to the financial statements, particularly in view of their substantial asset value.
-  The Ministry of Energy, which is expected to receive the authority of the Ministry of Water Resources, the Water Authority, the Companies Authority and Mekorot should settle their disputes and operates to remove the obstructions preventing the implementation of the government decision on sale of wastewater utilities, which constitutes an obstruction to the unification of the NWC assets stated in Mekorot books and to sale of the Mekorot real estate assets, and to the implementation of the program for the redemption of recovery water utilities. Those actions should be taken particularly in relation to recovery utilities that are not exempt from the obligation to conduct tenders according to the Ministry of Justice decision. Moreover, the Water Authority and Mekorot should push for a solution that will enable implementation of the government decision regarding the establishment of two companies for the wastewater treatment utilities in the Jezreel Valley and in the Hefer Valley under the conditions detailed in the government decision. If the government decision on certain issues cannot be implemented, it is recommended that the Ministry of Energy and the Companies Authority promote alternative solutions, including initiating a proposal to amend Government Decision 4514 on said issue, so that it can be implemented.



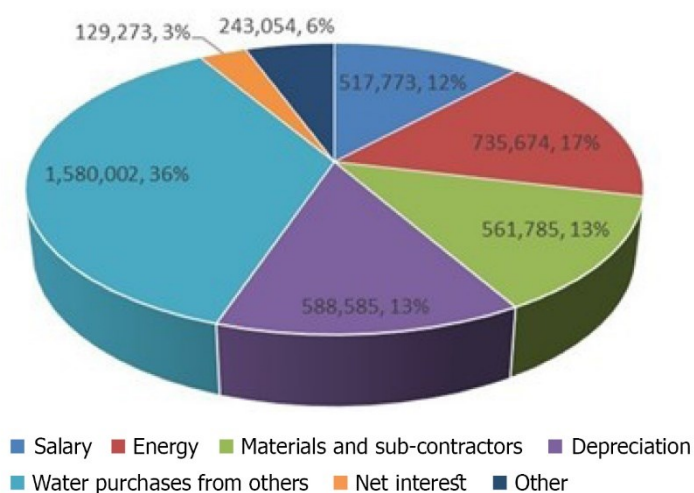


It is recommended that the Financial Resilience team meet at the frequency determined by its decision of December 2019. It would be appropriate for the implementation team, headed by the Ministry of Energy CEO, to whom the authority of the Water Resources Ministry are expected to be transferred, will continue to monitor the implementation of the government decision and act to advance it.



It is recommended that as part of the periodical update of the Mekorot tariff, the Water Authority Council examine the recognized costs calculation for the Company's financing costs. It is further recommended that the Companies Authority and Mekorot continue to examine from time to time the average life span of loans it takes. It is also recommended that the Financial Resilience Team continue to monitor the development of disparities between the set tariff interest and the actual interest paid by Mekorot, and discuss this matter.

### Segmentation of Mekorot expenses for 2020 (in thousands of NIS)







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## Summary

Mekorot is a government company with high and stable rating, whose bonds are traded on the stock exchange. However, it is facing many challenges, including a significant growth in the extent of the Company's development programs; its liabilities are 77% of the balance sheet; the debt coverage and leverage ratios are not as good as their ratios in similar companies in Israel and worldwide and even compared to its set goals. Most of the steps determined by Government decision 4514, intended for reinforcing Mekorot's financial resilience, have been performed or are in the process of being performed. The steps determined regarding wastewater treatment have not yet been implemented, despite constituting a condition for performing additional steps that are vital for its financial resilience. In view of the importance of Mekorot's financial resilience to the success of implementing the development program and due to the national importance of this program which is designed to prepare for prolonged periods of drought, the Ministry of Energy, to which the Water Resources Ministry authority are expected to transfer, the Water Authority, the Companies Authority and Mekorot should resolve their disputes and act to remove the obstructions preventing the implementation of these steps.





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Netivei Israel – The National  
Transportation Infrastructure  
Company Ltd.

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## **Inter-City Roads Maintenance – Follow-up Audit**









## Inter-City Roads Maintenance – Follow-up Audit

### Background

Netivei Israel – National Transportation Infrastructure Company Ltd (the Company or Netivei Israel) is a government company responsible for planning, developing and maintaining the network of inter-city roads in Israel and for the development of railway lines. The Company is responsible for an inventory of approximately 8,500 km of roads including all components – pavements, marking and painting, drainage, road signs and signposting – and including 9,000 road structures and bridges (in 2021, according to Netivei Israel's data).

Transportation infrastructure is of the utmost importance for the proper and efficient functioning of Israel's economy, and therefore the great importance of road maintenance and preventing neglect. The roads network serves as a vital infrastructure for all the residents of Israel, particularly periphery residents, and the maintenance activities contribute to ensure the road safety.

In 2017 the State Comptroller, published as part of Annual Report 68a a chapter on "The maintenance of inter-city roads" (the previous audit), in which the following deficiencies were detailed: reduction of the budget designated for road maintenance at Netivei Israel, the lack of supervision by the Ministry of Transport over road maintenance, the maintenance of pavements not according to a comprehensive plan, and more. The follow up audit indicated that since 2017 the Company has taken many actions to rectify the deficiencies presented in the previous audit and to improve the level of road maintenance regarding all components. However, since 2019 the budgets allocation to the Company for road maintenance works have decreased, and therefore there is a decrease in the scale of maintenance works performed.





### Key figures

<b>Approx. 8,500 km</b>	<b>x 5.4</b>	<b>x 3-3.5</b>	<b>Approx. 29%</b>
The length of roads, including all components, maintained by Netivei Israel (2019).	The growth rate in bridges and road structure inventory under Netivei Israel maintenance between years 2005–2021 (around 9,000 structures, of which 700 are bridges).	The growth rate in number of vehicles and mileage in 2018 compared to 1990.	The growth rate in length of roads under Netivei Israel maintenance between 2010 and 2018.
<b>NIS 1.1 billion</b>	<b>NIS 2.4 billion</b>	<b>Approx. 34%</b>	<b>Approx. 1% only</b>
The Netivei Israel budget for road maintenance, restoration and resurfacing for 2019.	The optimal maintenance budget required for Netivei Israel in 2019 according to the model it constructed.	A decrease in the updated maintenance budget for 2019 compared to the original budget according to the 2017 agreement.	The extent of expected road resurfacing in 2021 of the total roads network.

## Audit actions



From October 2020 to February 2021 the State Comptroller's office conducted a follow-up audit following the previous audit (the current audit or the follow up audit), where the actions taken by Netivei Israel to rectify the deficiencies raised in the previous audit were examined as well as the level of improvement following the rectification. This audit was conducted mainly at Netivei Israel, with supplementary examination at the Ministry of Transport and the Ministry of Finance.





## Key findings



**The Company's Road maintenance budget** – in the previous audit the State Comptroller's office recommended, among others, that "the Ministry of Transport and Ministry of Finance together with the company, examine whether the allocation of funds for road maintenance provides an appropriate solution to requirements". The follow up audit indicated that the actual updated road maintenance budget of Netivei Israel for 2017 and 2018 adhered to the agreed budget of 2016, and even higher; whereas the budget for 2019–2021 (same number of years) is significantly lower compared to the planned budget according to that agreed in 2016 – from an average of NIS 1,375 million to an average of NIS 1,106 million for these years (a decrease ranging from 4.72%–34.4%). It appears that this deficiency was not rectified by the follow up audit completion date.



**Maintenance of pavements and road resurfacing** – the previous audit indicated that: "In 2015–2016 the Company performed resurfacing works on 168 road segments, which are only 6% of the roads that do not adhere to standard pavement indexes as shown by pavement surveys performed by the Company. The Company budgets do not suit the road network requirements, and many road segments requiring maintenance are not included in the annual work plan". Moreover, the Company noted in the previous audit, that it wished to invest NIS 550 million in resurfacing, but in fact only NIS 238 million were approved. The follow up audit indicated that the extent of road resurfacing (in km) performed by the Company in 2020 dropped by 37% compared to 2017 – from 655 km to 410 km – and that the main reason for this is the absence of budget designated for road resurfacing. This trend is expected to continue in 2021, where the forecast drop for 2021 is even greater – a rate of 91% compared to 2017 – from 655 km to only 60 km – according to the total budgets allocated for this purpose at the audit completion date. It was found that this deficiency was not rectified by the follow up audit completion date.



**The Ministry of Transport supervision and control over bridge maintenance** – in the previous audit it was found that: "The Ministry of Transport did not deal with bridge maintenance and did not issue instructions for their maintenance. For this reason, the Company operates in this area without any professional support, and the professional instructions it prepared on the subject of bridge maintenance were not approved by any external entity". The follow up audit indicated that the Ministry of Transport has not yet prepared or initiated the preparation of instructions and procedures that regulate bridge maintenance. It should be stated that in the area of lighting and road marking the Ministry of Transport has set instructions and procedures. It was found that this deficiency was not rectified by the follow up audit completion date.





**Maintenance of lighting facilities** – the previous audit stated: "According to the Company data, the last survey on the matter was conducted in 2014 which showed that 580 junctions and over 1,200 segments are not illuminated according to these instructions [according to Ministry of Transport instructions from 1996]". The follow up audit found that the Company is handling road lighting according to an approved annual budget, and that the updated budget for maintaining lighting facilities for 2020 decreased by 27% compared to the updated budget for maintaining lighting facilities the previous year.



**Road markings** – the previous audit found that in November 2014 the Transportation Planning Department at the Ministry of Transport published directives for selecting and implementing standard materials for road marking. According to these directives Netivei Israel is required to use bi-component marking materials with long life spans or permanent sheeting with estimated durability of three to five years. The previous audit further indicated: "By audit completion date [previous] March 2017, the Company had not implemented the directives nor prepared for their implementation, mainly because no budgets had been allocated for this activity". The follow up audit found that at the follow up audit completion date the Company continued to use one-component ("simple") marking materials, mainly to renew the old existing markings. At the same time, it was said that the Company is acting in as much as possible to use bi-component marking materials in some of the new projects. The follow up audit indicated that this deficiency had been rectified only slightly, mainly due to the absence of budgeting for painting.



**The road maintenance projects transferred from local authorities to the Company responsibility** – the previous audit shows that the Company did not utilize of all the budgets allocated for this project during 2012–2016. In 2015–2016 this situation worsened as the project budgets increased significantly, but the performance rates were very low (45% and 35% accordingly). The follow up audit indicated that the Company fully utilized the budget allocated for maintenance of roads transferred to its responsibility from local authorities during 2018–2020, but there is a decrease in the level of the annual budget - from NIS 55 million in 2018 to NIS 15 million in 2020.



**Deficiencies rectified by Netivei Israel since the previous according to the budgets allocated for the performance of maintenance actions:**






- A. Adapting the bridges under its responsibility to earthquake resistant.
- B. Increasing lighting at junctions and unlit road segments; publication of a tender for replacing existing road lighting with led lighting, which is more environmentally friendly and with great savings potential.





- C. Using budgets to handle roads transferred from local authorities to the Company responsibility and roads that do not have a clearly defined entity responsible for maintenance.
- D. Activity to improve Company control of its maintenance actions.

## Key recommendations



-  The Ministry of Transport and the Ministry of Finance should formulate and approve the maintenance model as determined in Appendix E of the Operating and Financing Agreement. It should be stated that the budget allocation should also relate to the aspect of the major effect to be caused as a result of delaying preventive maintenance that may become breakdown maintenance, which will lead to higher costs compared to preventive maintenance.
-  The Company should continue to promote bridge maintenance on a regular basis, prioritize bridges with inferior maintenance conditions and present the Ministry of Transport and the Ministry of Finance with the importance of allocating appropriate budgets for bridges maintenance, both to prevent safety hazards and to reduce maintenance costs.
-  It is recommended that the Ministry of Transport and the Ministry of Finance examine the budget allocated for road resurfacing and adjust it to requirements. Incompatibility will in the future lead to higher costs for repairing roads, whereas the future saving exceeds the expected investment. An investment of NIS 1 will yield a future saving of NIS 2.76. According to the Company data, the lost benefit to the economy as a result of delaying maintenance actions for road resurfacing ranges between NIS 88 million and NIS 450 million<sup>1</sup>.
-  The Company should operate with the Ministry of Transport and the Ministry of Finance to allocate appropriate budgets for road lighting, due to the importance lighting facilities have in preventing severe road accidents in general and in unlit junctions in particular.
-  The Company, together with the Ministry of Transport and the Ministry of Finance should examine the road marking directives and decide on the allocation of an appropriate budget for their implementation. Marking roads with better quality materials may improve road safety and even lead to savings in the interim and long term.

<sup>1</sup> Depending on the various scenarios Netivei Israel presented to the State Comptroller during the follow up audit period, and according to the "Road Maintenance Budgeting Model 2019" document of September 2019. The scenarios present various frequencies of performing road resurfacing actions – between 8 to 10 years, which is a reasonable and worldwide common period of time for performing road resurfacing actions; between 10 to 12 years; between 12 to 14 years – according to the ratio of benefit for the economy and the resurfacing costs.





## The key findings of the follow-up audit – inter-city roads maintenance

Audit Chapter	The audited body	the deficiency raised in the previous report	The measure of deficiencies rectification raised in the follow up audit			
			Not rectified	slightly rectified	Considerably rectified	Fully rectified
<b>Netivei Israel Company road maintenance budget</b>	Ministry of Transport, Ministry of Finance	The Ministry of Transport and the Ministry of Finance, together with the Company, should examine whether the funds allocated for road maintenance provide an appropriate response to the Netivei Israel requirements. Moreover, they should examine whether the budget division between areas is optimal.				
<b>Pavement maintenance and road resurfacing</b>	Netivei Israel	In 2015–2016 the Company performed resurfacing works on 168 road segments, which are only 6% of the roads that do not adhere to standard measures, as shown by surveys conducted by the Company.				







Audit Chapter	The audited body	the deficiency raised in the previous report	The measure of deficiencies rectification raised in the follow up audit			
			Not rectified	slightly rectified	Considerably rectified	Fully rectified
	Netivei Israel	Around 20% of the roads included in the annual work plan are not determined by the Company surveys, but by professional entities in the various areas. No professional reasons for the selection process of these roads by the Company were found.				
Bridge maintenance	Netivei Israel	According to a Company review, deficiencies were found in many structures: 145 structures were categorized as "severe"; 517 structures were categorized as "very bad"; 442 were categorized as "bad".				
	Netivei Israel	In the earthquake resistance survey conducted by the Company in 2011, 72 bridges were rated under two severe categories. At the audit completion date, March 2017, the Company had restored two bridges only for earthquake resistance.				







Audit Chapter	The audited body	the deficiency raised in the previous report	The measure of deficiencies rectification raised in the follow up audit			
			Not rectified	slightly rectified	Considerably rectified	Fully rectified
	Ministry of Transport	The Ministry of Transport did not deal with bridges maintenance nor did it issue any directives for their maintenance. As a result, the Company operates in this field without any professional support and the professional directives it prepared have not been approved by any external entity.				
Maintaining lighting facilities	Netivei Israel	In the last survey on road lighting conducted in 2014 it was found that 580 junctions and over 1,200 road segments are not illuminated according to directives.				





Audit Chapter	The audited body	the deficiency raised in the previous report	The measure of deficiencies rectification raised in the follow up audit			
			Not rectified	slightly rectified	Considerably rectified	Fully rectified
Road painting	Netivei Israel	In November 2014 the Transportation Planning Department at the Ministry of Transport published directives for the selection and implementation of standardized products for road marking. By the audit completion date, March 2017, the Company had not implemented nor prepared to implement these directives because no budgets had been allocated for this activity.				
Supervision of contractors work	Netivei Israel	It was found that in July 2016, when the contract with the companies performing the integrated supervision expired, the Company ceased this activity.				





Audit Chapter	The audited body	the deficiency raised in the previous report	The measure of deficiencies rectification raised in the follow up audit			
			Not rectified	slightly rectified	Considerably rectified	Fully rectified
Maintenance of roads transferred from local authorities to the Company responsibility	Netivei Israel	The Company did not fully utilize the budgets allocated for this project during 2012–2016. In 2015–2016 this situation worsened: the project budgets increased significantly, but the performance rates were very low (45% and 35% accordingly).				
The road maintenance project with private sector participation	Netivei Israel	Although five years have already passed since commencing operation of the project, the Ministry of Transport and the Ministry of Finance have not yet performed any analysis to examine the advantages and disadvantages of the PFI model and its feasibility.				





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## Summary

Maintenance of roads, bridges and road structures is important on many aspects: road safety, preventing erosion of roads financial value and preventing greater future damage, advantages from saving in travel time of road users, etc. Road maintenance becomes more important in face of the increase in distances travelled and density of traffic on the roads, and due to the large investments made over the past decades, investments that have extended the roads and increased the number of bridges for maintenance. To perform maintenance activities an appropriate budget is required that will enable Netivei Israel to optimally maintain the transportation infrastructures.

The follow up audit indicated that the Company took action to rectify the deficiencies raised in the previous audit. Most of the deficiencies that were not rectified, derived from reduction in the maintenance budget allocated to the company by the Ministry of Transport and the Ministry of Finance.

As stated in the previous audit, the Ministry of Transport and the Ministry of Finance, together with the Company, should examine whether the allocations of funds for road maintenance provides an adequate solution to requirements, particularly in view of the new maintenance model developed by the Company in 2017. They should review whether budget division between the performance areas is optimal. These actions are vital for the Company to improve in the areas where the reality is disparate to necessity, particularly concerning pavements, road resurfacing, road markings and lighting. The Company should act to rectify the deficiencies in the maintenance of Hadera region according to the PFI model and consider feasibility of its expansion.









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Israel Tax Authority

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# **Exercise of Tax Benefits by the Tax Authority – Extended Follow-up Audit**









## Exercise of Tax Benefits by the Tax Authority – Extended Follow-up Audit

### Background

Non take-up of rights is a phenomenon whereby individuals entitled to benefits and certain rights do not exhaust them. Studies in various countries indicate the problem of non-exhaustion of rights in the fields of social security, such as receiving unemployment insurance fees, receiving tax benefits, ensuring income, compensation following work injury, and more. As for the exercise of tax benefits, it should be stated that only some of the public can enjoy certain tax benefits in the first place, among others due to income level or due to the manner of providing the benefit.

### Key figures

#### **76% of the deficiencies**

Raised in the previous report, were not rectified or only slightly rectified.

#### **NIS 1 billion**

The estimated excess taxes overpaid annually by the public. Only a minority of these taxpayers submit reports in order to receive the overpaid taxes.

#### **NIS 3.6 billion**

The estimated excess taxes paid by citizens that are not required to submit an annual report, in approximately 2 million cases, during 2016–2019.





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## Audit actions



The State Comptroller's Annual Report 66a, published in 2015 (previous audit) dealt with exhausting tax benefits at the Israel Tax Authority ("the authority"). From January to March 2021 the State Comptroller examined the rectification of the deficiencies by the Tax Authorities raised in the previous report and the implementation of the recommendations by the exercise of rights team established by the Tax Authority following publication of the report, and additional issues regarding the exhaustion of tax rights.





## First chapter – Follow-up of the rectification of the deficiencies raised in the previous audit

### Key figures

#### 37% of the recommendations

Of the committee for exhausting rights at the Tax Authority established following the previous report – were implemented. 28% were partially implemented, and 35% were not implemented.

#### NIS 12.2 billion

The Tax Authority charged for betterment tax, individual taxpayers that carried out real estate transactions, during 2016–2019.

#### 8.7% of betterment tax assessments

That stated spouses, separate assessment were issued during 2016–2019 for both spouses.

#### Only 4%

Of taxpayers under age 60 that requested layout of the capital gain (betterment) and to exercise the tax benefit, in 2016–2019.

#### NIS 9.7 million

3,831 citizens did not receive work grants between 2013 and 2019, for failing to update bank accounts.

#### 1,000 entitled

For a work grant for tax year 2013–2014, did not receive the grant and have been waiting for over 6 years.

#### NIS 670 million

The estimated excess tax collected from over 380,000 citizens that did not submit tax refund reports for 2014, which has expired.





## Key findings



### **Data collection and estimating for exercising rights and providing tax benefits**

– the previous audit raised that although the Authority has information on revenues of taxpayers, it does not have information that enables concluding how they exercise the tax benefits to which they are entitled, and that the Authority did not review the obstacles preventing the public from exercising their rights. The follow-up audit findings show that this deficiency was only slightly rectified, and that the Tax Authority did not act to receive all the information to enable it exercising taxpayers rights, including taxpayers that do not have to submit reports to the Tax Authority.



**Excess tax collection from employees** – the previous audit showed that when the Authority had information of monetary affect caused to citizens that did not exercise their rights, it did not initiate refund of these amounts and did not inform the citizens that according to its data they are entitled to a refund. The previous audit also found that the accrued amount of excess tax paid over the years by employees who worked in two jobs during the same tax year is estimated at several hundreds of millions of NIS. The follow-up audit findings indicate that this deficiency was not rectified, and that every year hundreds of thousands of families pay excess taxes for an extent of NIS one billion. The follow-up audit findings further indicated that hundreds of thousands of families that paid excess taxes do not submit tax refund reports at all and therefore do not exercise their rights. In addition, the follow-up audit found that as of February 2021, according to the Tax Authority calculations for tax years 2013–2019 it owes in approximately 2 million cases (individuals that are not obliged to submit annual income tax reports) a total estimated amount of NIS 3.6 billion. This population of employees includes, for instance, employees that reported working in two jobs, paid maximum tax rates, but did not adjust the taxes; employees that worked part of the tax year and did not submit a refund report for excess tax payment. The follow-up audit also indicated that other than the pilot performed by the Tax Authority in 2015, within which it sent 1,700 letters to alleged entitled who overpaid tax, the Authority did not take action on an annual basis to refund the excess taxes collected.





**Exercising tax benefits entailed in deposits for pension savings** – the previous audit indicated that the method of calculating benefits due to deposits for pension savings is complicated, employees that do not understand the substance of the benefit offered are not expected to use it and the Authority has not developed computerized tools for exercising the benefits within the family unit. The follow-up audit findings show that the deficiencies were not rectified, including the finding regarding the fact that at the time of submitting tax refund reports, the Authority did not provide the public with tools to assist it in registration of the family deposits to pension funds on the tax refund






forms, in a manner that would benefit the family (by increasing the family tax return or decreasing tax liability). Moreover, the Authority did not develop computerized tools to present the full tax saving potential from deposits to provident funds that would assist taxpayers when submitting reports.

 **Locating citizens with credit balances** – the previous audit showed that the Tax Authority frequently does not transfer to individuals (citizens that are not obliged to submit reports) the credit balances accrued. Whether due to lack of updated bank details, or whether due to the need to take action for locating the eligible. The follow-up audit findings indicate that the deficiency was only slightly rectified. However, the Tax Authority notified the State Comptroller's Office that in 2020 it had refreshed the instruction concerning the obligation to input bank details to the tax authority computers as stated by the submitters of tax refund reports, particularly when the Authority does not have the bank details of report submitters. Moreover, although the Tax Authority has verified over a million bank accounts, there are approximately half a million accounts that have not yet been verified, and as a result there is no updated information concerning bank account details of all citizens.

 **Handling credit balances of citizens entitled to work grants** – as of March 2021 3,831 individuals entitled to work grants for tax years 2013–2019 have not yet received their grants, due to their bank accounts not being updated in the Tax Authority computers. It should be noted that at the beginning of 2021 the Tax Authority updated bank accounts of 856 (18%) of the eligible enabling transfer of the grant to their accounts. The follow-up audit also raised that as of March 2021 there is a credit balance of NIS 9.7 million in favor of the entitled individuals with missing updated bank accounts details.

 **Exercising betterment rights** – the previous audit indicated that the tax benefits, such as allowing a payment dispensation of betterment (attributing the income from capital gains over several tax years) and its division between both spouses of the family, designed to reduce the family's tax liability, are not exercised. The follow-up audit findings indicated that five (50%) out of ten deficiencies relating to aspects of services in handling applications for payment dispensation of betterment tax payments were fully or to a great extent rectified. However, five (50%) of the ten deficiencies relating to exercising rights entailed in the payment of betterment tax were not rectified or only slightly rectified. For example, only a small part of taxpayers obliged to pay betterment tax (11% of age 60 and over and 4% under age 60) submitted an application for a payment plan the capital gain, did not offset the capital gain against other capital losses and only a few (2,338 additional assessments were performed to spouses out of 188,755 taxable betterment land assessments) shared the capital gain between both spouses partners to the land transaction, and the Authority on its behalf did not provide the citizens with a simulator to assist them in exercising their rights.





The audit also found that evident that between 2016–2019 the potential betterment that can be shared between spouses on land transactions was estimated at NIS 20 billion, due also to the fact that 67% of women (wives) do not reach income tax threshold, or they are unemployed – and remain with unused credit points that can be offset against betterment. Therefore, there is concern that some individuals paid excess betterment tax, derived from non-exhaustion of tax rights entailed in sharing the betterment between spouses.



**Exercising retirement rights** – the follow-up audit findings indicate that the Authority did not complete establishing a consulting body that would clarify to workers over the course of retirement, the taxation alternatives available for pension savings, and therefore many retirees are not aware of these alternatives.



**Tax loss due to tax year statute of limitations** – approximately 380,000 individuals or families that are not obliged to file annual income tax reports have lost a total amount of NIS 670 million for tax year 2014 because of not filing tax refund reports. Based on 2014 data, it can be assumed that public losses (individuals or families not obliged to file annual income tax reports) have totaled billions of NIS over the years. The audit also found that as of 2021, 435,546 families have not yet filed income tax reports for tax year 2016. The tax refund these families are entitled to is estimated at NIS 803 million. According to the law, if no tax refund report is submitted to the Tax Authority for this year by the end of tax year 2022, the families will lose this amount.



**Implementing the recommendations of the Tax Authority Committee for Exercising Rights** – as of March 2021 the Tax Authority implemented 19 (37%) of the 51 recommendations of the Tax Authority Committee for Exercising Rights reviewed by the State Comptroller's Office. It was also found that 14 (28%) of the recommendations were only partially implemented, and 18 recommendations were not implemented at all.



**Exercising rights of persons with disabilities and holocaust survivors** – the Tax Authority has acted to promote exercising the rights of holocaust survivors and of parents to children with disabilities.

**Pension continuity for retirees** – the follow-up audit findings concerning time limitation for selecting an alternative of retirement grant indicate that the deficiency was rectified in 2017. As part of Amendment 232 to the Income Tax Ordinance an article was added to section 9(7a)g1) according to which an employee that retired and the amounts available at his disposal in the compensation component do not exceed the section ceiling, shall be regarded as having submitted a request for pension continuity, unless requested otherwise.





## Key recommendations



**Exercising rights of citizens not obliged to file annual reports** – it is recommended that the Tax Authority act to exercise the rights of citizens that are not obliged to file annual income tax reports on all relevant matters.



**Refund of excess paid taxes** – it is recommended that the Tax Authority carry out a detailed mapping of excess paid taxes, giving priority to those paid in early years and to the subjects on which there is reasonably high certainty of excess paid tax. It is further recommended that the Authority initiate an approach to taxpayers and provide them the data concerning excess payment of tax they made and instruct them on how to exercise their rights to a refund.



**Exercising rights on pension savings** – it is recommended that the Tax Authority act to exercise all family rights to pension savings according to the Ordinance. It is further recommended that the Tax Authority act as much as possible to develop appropriate professional tools, including computerized tools, to enable taxpayers that are not represented to exercise their full rights. Moreover, in view of the importance of tax benefits on pensions and in view of the complexity of the matter, it is recommended that the Tax Authority provide the public with appropriate professional tools that will award taxpayers with comprehensive information on the subject of exercising pension rights, such as a pension deposits calculator, that will assist families in exercising their full rights to tax benefits. This will act as an incentive to the public for savings and will increase their financial security during their pension years.



**Exercising rights in real estate taxation** – it is recommended that the Tax Authority act to exercise taxpayer's rights concerning the refunding of excess betterment tax; act to locate cases where the seller of an asset or their spouse did not exercise their rights to lower tax rates or their tax credit points to which they are entitled, and inform them of their alleged entitlement to betterment tax refund. It is also recommended that the Authority locate taxpayers that according to its data, have accrued capital losses, and inform them that betterment can be offset against capital losses. It is further recommended that the Authority provide its employees with a computerized system for calculating betterment payment dispensing, and provide the taxpayers and their representatives a simulator of this system, to assist them in making decisions on the feasibility of dispensing betterment amounts and on the best way of dividing betterment between spouses in the family.



**The establishment of a consulting body for retirees** – it is recommended that the Authority complete writing the retirement manual and publish it alongside preparing a





simulator that will be available to the public. It is further recommended that the Ministry of Finance review the possibility of establishing a retirement consultation center.



**Formulating a list of tax benefits and acting towards their realization** – it is recommended that the Tax Authority join the "National Rights Engine" project, and for this purpose formulate a list of all the tax benefits taxpayers of all sectors can enjoy, and in addition, formulate a separate list of all potentially entitled taxpayers to all tax benefits, which will constitute a basis for establishing a tax simulator to enable taxpayers to exercise all their rights.



**Easing the bureaucratic burden imposed on persons with disabilities** – it is recommended that the Ministry of Welfare and Social Affairs and the "Egov" Department at the Government ICT Authority act to complete the project for issuing digital blind certificates thereby assisting persons with disabilities to exercise their rights for tax benefits, and ease the burden imposed on these persons when exercising their rights.





## second chapter – Aspects of exercising rights and tax benefits

### Key figures

#### 54% of individuals

(Employees and self-employed) do not reach tax threshold, and cannot enjoy the tax benefits. As of tax year 2019.

#### 67% of women

And 44% of men do not reach tax threshold and to not enjoy the tax benefits they are entitled to.

#### In 50% of the families

Where both spouses work, credit points awarded to women are not exercised or only partially exercised.

#### NIS 2,330 million

The estimated tax benefits for residents of beneficial settlements in 2019.

#### NIS 28 billion

Total evaluated tax benefits for pension savings in 2019.

#### 41%

Of the total tax benefits for pension savings received by top decile employees. 1.6% are received by employees in the four low deciles.

#### NIS 900 million

Received by top percentile employees as tax benefits for deposits in pension savings, whereas the four low deciles received NIS 370 million, for tax year 2019.

#### 54 employers

At most, had given a permission to their employees to receive tax credits for donations through their paychecks During 2015–2019.





## Key findings



**Promoting social objectives by giving tax benefits** – in 2018 and 2019 the rate of employees whose income was lower than the tax threshold (do not pay taxes because of their low income and personal details) was 57%, compared to the rate of self-employed whose income was lower than the minimum taxable income which was 40%. The audit also found that the income of 67% of women was lower than the tax threshold. The income of 44% of men was lower than the tax threshold. As a result, they are potentially unable to enjoy the tax benefits.



**Tax coordination on the Internet** – the audit found that there are taxpayers unable to perform tax a coordination via the Internet, and can do so only via the regional assessment office. For example: Persons requesting special tax exemptions, including exemptions for pension; persons who reached pension entitled age before validity of Ordinance Amendment 190 and owe tax on all income; new immigrants; returning residents; persons awarded tax benefits such as 100% disability or sight impaired; persons with credits from donations to recognized institutions.



**Tax benefits due to consolidated family calculation** – for spouses that are not required to submit annual income tax reports it appears that the Authority does not perform hindsight calculations to verify that the family received all the tax benefits it is entitled to. Moreover, after receiving employer reports the Authority does not perform calculations to verify whether tax benefits were exercised, and to determine the reporting channel that would be better for the family – separate or consolidated reporting. Moreover, the authority does not inform the taxpayers if they are entitled to tax refunds for overpayments, and thereby does not allow them to exercise their rights by filing reports for tax refunds.



**Exercising credit points of new immigrants and returning residents** – the audit indicates that the Authority does not have data regarding the number of new immigrants and returning residents that are entitled to credit points, and of those eligible that did not do so. As a result, it is not possible to inform those eligible of rights not used, and the Authority on its behalf is not able to credit them.



**Exercising tax benefits on deposits to pension savings by deciles** – lower decile employees do not reach the tax threshold and cannot exercise the benefits entailed in deposits for pension savings.





**Exercising tax benefits for donations** – for each of the years 2015–2019, approximately 54 employers at most of the employers registered at the Tax Authority exercised each year their prerogatives as employers, and enabled their employees to





receive tax credits for donations to recognized public institutions through their paychecks. The audit also found that the simulator installed on the Authority website does not indicate to taxpayers that the amount inputted as their and their spouses donations, does not grant the optimal tax benefits receivable by dividing donations between spouses.


 **The commencement of entitlement to tax benefits in national priority settlements** – having failed to publish the peripheral index on the date originally determined by law, January 2017, there has been a substantial delay in validation of entitlement to tax benefits of approximately two hundred settlements entitled to benefits according to the outline of the Benefits Law, home to 700,000 capita, due to the fact that their entitlement became valid in 2018 instead of 2017.


 **An active mechanism for exercising rights** – the Authority does not have an active mechanism for exercising social rights with direct interfaces to target populations. Had there been such a mechanism available it would have been able to establish a process of providing service of reaching out its services to target populations.



**Automatic approvals for tax coordination** – in preparation for tax year 2020, the Tax Authority sent automatic approvals for tax coordination for the new year to 300,000 employees thereby saving them the need to perform a new tax coordination. The Authority also sent a letter to 73,000 pensioners who fixed their rights in the calculation of their allocated pension, regarding the updating of the exemption rate they are entitled for the regular monthly pension.

## Key recommendations

 **Increasing progressivity in tax benefits for pension savings** – it is recommended that the Authority, in coordination with the Capital Market Authority and the "Digital Israel" staff, complete the examination of the "Leaving the Workplace" project and include it in the Authority's annual work programs, including setting a schedule for its implementation.

 **Developing digital applications to exercise rights** – it is recommended that the Tax Authority examine promoting processes for developing digital applications that will allow citizens to exercise their rights regarding all matters discussed in the follow-up audit, to locate data mistakes in their affairs, and to permanently update their details. It is recommended that the Authority provide to the public information regarding all rights it is entitled, simply and clearly, accompanied by explanations and instructions, in order to assist the public to exercise its right and reduce its tax liability.





**The declarative reporting model for promoting exercise of rights** – it is recommended that the Ministry of Finance in coordination with the Tax Authority examine the possibility of implementing the declarative reporting model in Israel, among others through learning and drawing conclusions from implementation of this model worldwide. This model, combined with the use of internet and cellular platforms, may expand the extent of exercising rights of all taxpayers, and particularly rights of disadvantaged populations.

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## Summary

The grossed up financial extent derives from taxpayers not fully exercise their rights and the excess tax collected is estimated at several billions of NIS. The audit findings show that the Tax Authority does not fully initiate provision of these rights to those entitled; among others the Authority does not act to provide full and transparent information to the public, particularly information concerning the existence of the right to exercise various tax benefits and the conditions for receiving those rights. The audit also found that the Authority did not promote removal of the bureaucratic burden imposed on citizens wishing to exercise their rights – rights in tax return reports, rights in betterment payments and rights of retirees. The Authority also did not promote the handling of overpayments made by the public to the Tax Authority.

The Authority did act to assist persons with disabilities, parent of a child with a disability and holocaust survivors to exercise their rights. The Tax Authority must initiate on-line steps for exercising citizens' rights, with supervision and control. It is recommended that the Authority include within those steps an examination of the extent of non-take-up of rights, and what are the obstructions contributing to its occurrence.





### The level of rectification of deficiencies stated in the previous audit

The Chapter	Estimates – Absence of estimates and monitoring the rate of exercising tax benefits	Not rectified	Slightly rectified	considerably rectified	Fully rectified
<b>Estimates – Absence of estimates and monitoring the rate of exercising tax benefits</b>	Despite the Authority having information on taxpayers income, it does not have information to conclude how they exercise their entitled tax benefits.				
	The Authority did not review the obstruction preventing the public from exercising their rights.				
	As part of the Authority's work plans it did not include reviewing the rate of exercising tax benefits.				
<b>Losses due to surplus tax collection</b>	Even when the Authority had information concerning monetary injury to citizens that did not exercise their rights, it did not take initiative to refund these amounts, and did not inform them of their entitlement to a refund according to its data.				
	Surplus tax collected from employees that did not work an entire year.				
	The accumulated amount of surplus tax paid over the years by employees working at two work places during the same tax year is estimated at several hundreds of millions of NIS.				



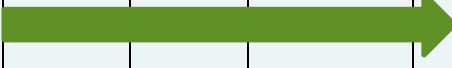
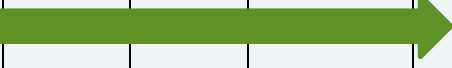

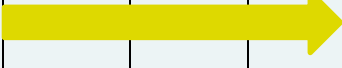




The Chapter	Estimates – Absence of estimates and monitoring the rate of exercising tax benefits	Not rectified	Slightly rectified	considerably rectified	Fully rectified
<b>Non-take-up of benefits on deposits for pension savings</b>	The method of calculating benefits for deposits to pensions savings is complex.				
	Encouraging deposits for pension savings – workers that do not understand the benefit substance are not expected to take advantage thereof.				
	Non-take-up of tax benefits for families deposits to pension funds.				
	Non-development of computerized tools to enhance family deposits.				
<b>Non-take-up of benefits for the matter of betterment tax</b>	Only some citizens that paid betterment tax asked for dispensation of the capital gain, which could have reduced the tax liability for some of them.				
	Non offsetting of capital gains and utilization of personal credit points against betterment tax paid.				
	At the time of selling rights in land by two spouses the Land Taxation Office issues the assessment on the name of the registered spouse only, and the betterment assessment determined by the Land Taxation Office does not benefit the family.				











The Chapter	Estimates – Absence of estimates and monitoring the rate of exercising tax benefits	Not rectified	Slightly rectified	considerably rectified	Fully rectified
	In few cases the family requested dividing the capital gain (betterment) between the two spouses, as part of the real-estate property sale.				
	The Authority directives do not determine means for monitoring transfer of taxpayer applications for betterment dispensation from the Assessment Office to the Land Taxation Office.				
	The Assessment Offices delay transfer of the betterment payments dispensation applications to the Land Taxation Offices.				
	The land taxation Offices delay handling the applications for betterment payments dispensation transferred from the Assessment Offices upon their arrival.				
	The connection between the Income Tax Offices and the Land Taxation Offices is deficient concerning handling of betterment payments dispensation.				
	Most of the land taxation employees, the Land Taxation workers do not have access authorization to data used to determine the income tax assessment.				





The Chapter	Estimates – Absence of estimates and monitoring the rate of exercising tax benefits	Not rectified	Slightly rectified	considerably rectified	Fully rectified
	The Authority did not provide its employees, or the public, with a computerized system (simulator) that would assist in calculating the betterment tax through capital gain dispensation.				
<b>Refund of credit balances to the public</b>	The Assessment Offices do not initiate any actual actions to locate persons entitled to tax refunds whose bank account details are not updated in the Tax Authority databases.				
<b>Handling of pensioners</b>	<p>The public is not well versed in the taxation alternatives available at retirement, and does not have sufficient information on the subject.</p> <p>Taxpayers are allocated a limited time to select the taxation alternatives of retirement grants, and once the taxpayers have made their decision on the subject, they are not entitled to change it.</p> <p>If the employee did not select the option of continuous pension, he was not entitled to continuous pension.</p> <p>The Tax Authority did not provide the public a retirement simulator for use.</p>	   			





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The Government Water and Sewage  
Authority

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# **Preventing and Monitoring Pollution and Salination of Water Sources, and their Recovery**







## Preventing and Monitoring Pollution and Salination of Water Sources, and their Recovery

### Background

Ground water is a primary strategic source of water worldwide: providing almost half of the world population's drinking water and around 40% of water for agriculture. Ground water provides the main supply of clear, natural water for Israel's water sector. There are two major ground water aquifers in Israel – the coastal aquifer and the Yarkon Taninim aquifer (also known as the mountain aquifer). Israel's natural water sources and particularly ground water are in increasing danger of pollution and salination as a result of industrial activity, fuels, agricultural activity and over-pumping of the various aquifers, which causes their levels to drop and allowing salinized water to infiltrate. The Government Water and Sewage Authority is in charge of maintaining the quality of natural and artificial water sources, of their recovery, improvement and is responsible for preventing their pollution.





## Key figures

**2.24****billion m<sup>3</sup>  
1**

Total water consumption in Israel for 2019.

**17**

The number of fuel container farms that are unmonitored (out of a total 35 farms) as of November 2020.

**2.3****billion m<sup>3</sup>**The total known volume of polluted water, which is 6.5% of the coastal aquifer (that has a total volume of 35 billion m<sup>3</sup>) as of 2020.**NIS 1****Billion**The recovery costs of three sites where IMI was active<sup>2</sup>, according to an estimate from 2015.<sup>3</sup>**72%**

The rate of sites out of 130 sites polluted with dissolved fuel that are in process of recovery, as of November 2020.

**8.3%**The rate of monitored industrial areas out of all industrial areas in Israel<sup>4</sup>; at 77% of the sites with industrial pollution no recovery actions have been taken<sup>5</sup>, as of November 2020.**13.5%**

The rate of monitored fuel facilities out of 2,184 known fuel facilities; at 79% pollution was found, as of November 2020.

**21%**

The rate of sites out of 130 sites polluted with dissolved fuel that are in process of recovery, as of November 2020.

**Audit actions**

From June to December 2020 the State Comptroller's Office examined the actions taken by the Government Water and Sewage Authority, the Ministry of Environmental Protection, the Ministry of Defense, the Nezer Sharon Company Ltd. and the Ministry of Finance in order to monitor Israel's natural water sources, to prevent their pollution and

1 Cubic meter.

2 The Israeli Military Industry Ltd – IMI.

3 The Water Authority informed the State Comptroller's Office that this financial data will be updated in the coming year.

4 It should be stated that among all the industrial areas, there are areas that do not involve operations that constitute a risk of polluting water sources.

5 Sites where industrial pollution has been found and where no recovery actions have been taken are in various stages of investigation regarding the extent and nature of the pollution, monitoring for the purpose of decision making on the need for recovery or in preparation for recovery.



promote their recovery, with focus on ground water reserves. Supplementary examinations were conducted at the Ministry of Health.

## Key findings



**Regulation in the field of fuel pollution originating at container farms** – despite the importance of fuel container farms, and in view of the immense potential for damage deriving from their use including severely high fuel pollution, the establishment of regulations to prevent pollution from fuel container farms has not been completed even though a draft in this regard was published in 2004.



**Monitoring and mapping the pollution of natural water sources** – at 98 (24%) of the 408 monitored sites recovery actions have been or are being performed and at only 12 sites (3%) the recovery operations have been concluded. At 48 (12%) of the sites the Water Authority found that there was no pollution that required additional action. At the remaining 262 monitored sites – 64% of all monitored sites – there are signs of existing pollution or suspected pollution.



**Monitoring of the Yarkon Taninim aquifer and the other aquifers compared to monitoring of the coastal aquifer** – most industrial monitoring is performed on the coastal aquifer (21 out of 157 industrial areas are located above the coastal aquifer). It appears that there are no significant industrial monitoring activities of the Yar-Tan aquifer. In the field of industrial originated pollution, no monitoring sites have been established in recent years on the Yar-Tan aquifer, and all monitored industrial areas are located above the coastal aquifer.



**Monitoring pollution from fuels** – at 69% of the monitored sites, 203 in all, pollution was discovered in the water source, and at 36% of the monitored sites severe and very severe pollutions were found. In addition, monitoring actions performed at 295 sites from 1999 to 2020 constitute a coverage of 13.5% of all known sites. Despite fuel farms being responsible for the major portion of pollution from fuel facilities, 17 out of the 35 container farms have not yet been monitored, which means that the potential for severe pollution (fuel lenses) from fuels may be significantly higher than the known extent.



**Monitoring industrial pollution** – 12 years have lapsed since the publication of the Tahal report<sup>6</sup> which indicated a high potential for pollution at 23 industrial areas ; as of the audit completion date two of these industrial areas have not yet been monitored. It was further shown that of the 157 industrial areas above the coastal aquifer and out of

6 Tahal, the Israel Water Planning Company Ltd, submitted a summary report in November 2008, to the Water Department at the Water Authority, on the subject of a monitoring plan for selected industrial areas on the coastal aquifer.





the total of 253 industrial areas in Israel, 21 industrial areas that are high risk (8.3% of the total industrial areas), are monitored.

**Recovery of fuel pollutions in natural water sources** – out of 261 fuel sites – where recovery actions were or may be required, recovery actions at only 8 (3%) of the 261 sites have been concluded. As for the remaining 253 sites, at 77 (30%) recovery activities are currently being performed. The result of this situation is that in addition to the low monitoring rates, the recovery rates of sites already monitored are low and does not provide a solution to the existing and potential extent of pollution from fuels in the ground water. Moreover, the Water Authority does not have a plan for the recovery of polluted sites.

**Handling sites where ground water pollution derives from the activity of IMI and the Defense Establishment** – at 12 of these 14 sites recovery actions have not yet been performed despite the large pollution extent totaling 1.4 billion m<sup>3</sup> and the presence of various dangerous pollutants, and although a long time has passed since the commencement of investigation to determine the pollution extent and to monitor and detect pollutions. It should be noted that at the major polluted centers, where a volume of over 1.2 billion m<sup>3</sup> of polluted water was discovered – IMI Ramat Hasharon, IMI Givon, IMI Magen and IMI Arvei Nahal – the pollution was discovered ten or more years ago, and at IMI Nof Yam, IMI Tirat Hacarmel and <sup>7</sup> the Tel Hashomer Recovery and Maintenance Unit, pollution was discovered five or more years ago. Moreover, it was found that at four of the 14 sites no initial investigation was carried out and there is no source for financing such investigation.

**The Water Authority's use of corrective orders** – the Water Authority limits its use of corrective orders, which allow it to order the polluters to take all required measures to stop water pollution, including recovery through restoration to the pre-pollution state and to prevent recurrence of water pollution. It does not allocate an appropriate part of its budget for treating pollution, despite being expected to collect these funds from the polluters. At industrial areas two disfiguration amendment orders have been issued over the past ten years, despite the scores of extensive and severe pollution epicenters that are not treated, and although some were discovered over 15 years ago.

**Improving the efficiency of the use of nitrates** – although there is an increase in the concentration of nitrates in Israel's coastal aquifer and Israel is positioned high on the scale of average nitrate quantity per area compared to OECD countries, the relevant bodies – the Ministry of Agriculture, the Ministry of Environmental Protection and the Water Authority – have not yet formulated a plan to reduce and improve the efficiency of the use of nitrates. Failure to take action may lead to the continued spread of pollutants and to the closure of additional water wells.

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<sup>7</sup> Recovery and maintenance center










**Monitoring industrial areas with high pollution potential** – the Water Authority is acting to monitor the industrial areas of Kiryat Arye and Ramat Siv, which were defined 12 years ago as having high pollution potential.

**Preparations for treating pollutions originating from IMI activity in Ramat Hasharon** – a joint tender committee of the Accountant General, the Water Resources Ministry and the Water Authority was formed to promote an international tender for planning, establishing and operating a facility to treat polluted ground water to be pumped from polluted areas at the IMI compound in Ramat Hasharon.

## Key recommendations

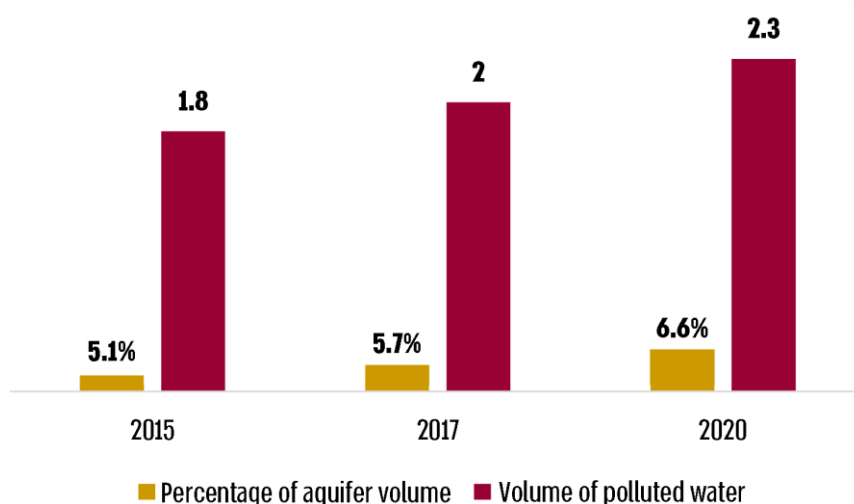
-  It is recommended that the Water Authority examine the possibility of increasing its fuel monitoring setup, formulate a multi-year monitoring plan and initiate together with the Ministry of Environmental Protection and the local authorities a mapping process of unauthorized fuel facilities and monitoring thereof.
-  It is recommended that the Water Authority promote the preparation of a comprehensive and overall monitoring plan that will enable the establishment of an effective monitoring setup, including the detection of pirate (unauthorized) fuel facilities and focusing on monitoring container farms, and act to receive information on the extent of pollutions originating from the Palestinian Authority territories. It is also recommended that the Authority conduct a survey for assessing the potential risk and pollution of the Yar-Tan aquifer and of other aquifers.
-  It is recommended that the Water Authority, the Ministry of Agriculture and the Ministry of Environmental Protection promote the formulation and implementation of a plan to improve the efficiency and reduce the use of fertilizers, paying attention to the actions taken by OECD countries in this matter and to the possible effect on the extent of agricultural activity and formulate a suitable solution, in order to reduce nitrate damage to ground water.
-  It is recommended that the Water Authority act to formulate a recovery plan for sites polluted by industrial activity while examining the benefits in relation to all sites where pollution was discovered, and to increase the recovery actions at fuel polluted sites. According to the findings from monitoring all fuel farms, the Authority should act to recover the fuel-derived pollutions.
-  It is recommended that the Ministry of Defense, the Ministry of Finance, the Companies Authority, the Nezer Sharon Company and the Water Authority cooperate to resolve their disputes concerning responsibility for performing and financing pollution recovery actions from the IMI activity, including: financing recovery actions, complete pollution





investigations, preparation of and carrying out a recovery program, with a set budget and schedule for executing the project. If the disputes are unbridgeable, it is recommended to bring this issue for the decision of the Government Attorney General.

### Volume of polluted water (billion m<sup>3</sup>) and its percentage of the total aquifer volume



Source: The Water Authority.

## Summary

Past activities of defense industries and of IDF bases are the major cause of pollution in the coastal aquifer, which is a vital source of supply of clear water for Israel's water sector. The Water Authority, the Ministry of Finance and the Ministry of Defense, which are the bodies responsible for treating pollution, especially those originated from the activity of the defense industries and IDF bases, have not yet completed recovery actions to treat the pollution. The bodies concerned – the Water Authority, the Ministry of Defense, the Ministry of Finance, the Ministry of Environmental Protection and the Ministry of Agriculture and Village Development – should act to rectify the deficiencies detailed in this report and examine the implementation of its recommendations, including formulation of a multi-year plan to treat pollutions, allocating appropriate budget according to predetermined priorities and operate to remove pollutants from the various aquifers.





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Israel Electric corporation Ltd.

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# **Debt Management at Israel Electricity Corporation Ltd.**









## Debt Management at Israel Electricity Corporation Ltd.

### Background

The Israel Electricity Corporation Ltd (IEC) is a government and public company, with 99.85% of its shares held by the Israeli Government. The company generates electricity and provides it to all sectors of the Israeli economy. At the beginning of the previous decade the IEC faced a severe crisis following cessation of natural gas supplies from Egypt. The crisis reached its peak in 2012 and was one of the causes of severe deterioration in the company's financial position: its net financial debt totaled approximately NIS 52 billion, however since then there has been a significant improvement in its financial position. In 2018 two agreements were signed – an assets settlement between the State and the IEC and a structural change of the electricity sector arrangement (the electricity sector reform). One of the main principles of the reform is strengthening the IEC's financial position. These agreements brought a further reduction in the company's debt and improved its financial resilience.





## Key figures

**NIS 36  
billion**

The IEC net financial debt in December 2019. In December 2020<sup>1</sup> – the debt decreased to NIS 30 billion, a decrease of 42.3% compared to its level in 2012.

**69%**

The actual leverage rate<sup>2</sup> at the IEC in 2020, and 72% in 2019. The financial leverage rate<sup>3</sup> in 2020 totaled 57% compared to 62% in 2019.

**4.4**

The debt ratio to EBITDA<sup>4</sup> in 2019 compared to a ratio of 8 in 2013. In 2020 the ratio was 3.99.

**3.79%**


The average interest rate on debt capital<sup>5</sup> in 2019. In 2020 the average interest rate was 3.49%.

- 1 The debt includes revenue's surplus following sale of the Ramat Hovav power generation plant – a total of NIS 2.433 billion.
- 2 Debt capital relative to the balance sheet.
- 3 The ratio between the financial debt and the financial debt with added owners' equity.
- 4 This index is not based on accepted accounting practices, and therefore there may be changes in the index values calculated by various bodies. The debt ratio to EBITDA in 2019 totaled 4.4 according to the IEC data compared to 5 according to the S&P rating company data. In 2018 the ratio was 4.82 according to the IEC data, but was 5.6 according to the Government Companies Authority data (which took the gross debt to EBITDA into account. The IEC relied on the net debt). In this report we have presented data from various sources and we have used the data from the same source to indicate trends.
- 5 Capital from external sources.



50%	61%	NIS 5.9 billion	BBB
The rate of debt in 2019 held by IEC out of the total company's debt issued in interest rate of 5% or more.	The rate of decrease in debt from 2012–2019 due to tariff return. Of which 46% derived from return of costs caused by the fuels crisis and 15% from advance tariff payments given to IEC by the Electricity Authority. Alongside this, 17% of the decrease is explained by the assets settlement between the company and the State, 6% from sale of the Alon Tavor power plant, and the remaining decrease (16%) from additional actions taken by the IEC.	The safety cushion held by IEC in December 2019. In December 2020 IEC held a safety cushion of NIS 6.46 billion.	The IEC international credit rating according to S&P company. The rating is higher by four notches <sup>6</sup> than the Stand Alone Credit Profile (SACP) of IEC, bb-.

## Audit actions

 From April to December 2020 the State Comptroller's office audited the debt management at IEC. Among others, the actions taken by the IEC and the regulators to decrease the debt and reduce its costs were examined. The audit was carried out at the IEC, the Electricity Authority and the Government Companies Authority.

## Key findings



**The IEC risk level** – despite the improvement in the IEC's financial position between 2012–2019, the company's risk is perceived as high compared to that in similar electricity companies in Europe.

**Factors contributing to decrease in the IEC debt** – the decrease in debt and improvement in the financial position of the IEC over the past decade were achieved mainly as a result of tariff returns due to the fuels crisis and advance payments the company received from the Electricity Authority (total 61% of the decrease). The assets

<sup>6</sup> The credit rating is divided into levels and each level is called a notch.





settlement contributed additional 17% to the decrease in debt, and sale of the Alon Tavor power plant provided further decrease of 6%. These actions together contributed in total 84% of the total decrease in debt. The remaining decrease is explained by actions taken by the company, most of which were at the expense of developing the electricity sector. This signifies that the decrease in debt is explained mainly due to disposable measures and not as a result of steps that are part of the company's ongoing operating activities.

**The interest rates in the company's bonds series at end of 2019** – 12% of the company's bonds issued at a high interest rate of 7% – an interest rate that is much higher than the interest rate of bonds issued by the company in 2018, which decreased over the years following the improvements in the company's financial position and as a result of the relatively low interest rate in the financial markets. Half of the company's debt carries an interest rate of over 5%, which is twice the marginal interest rate in 2018.

**Resources allocated by IEC to improve its financial position from 2012–2019 and the development plan for 2018–2022** – the planned investments for 2018–2022 total an average of NIS 3.2 billion annually. This level of investments is lower than the average of investments planned for 2013–2017, which totaled an average NIS 5.09 billion annually (for the maximum investments alternative) and are slightly higher than the minimal investments alternative set to reach an average annual investment of NIS 2.9 billion. Yet, the average investments between 2013–2017 was partial and totaled only NIS 1.8 billion annually. This indicates that the planned level of investments does not, therefore, compensate for the sub-investments in the previous development plan and it is doubtful whether the current development plan provides a sufficient response to the needs of the electricity sector. The audit raised a concern that the company is expected to fulfill the goals defined within the reform and the goals set by the board of directors, inter alia by postponing important projects.

**The IEC's safety cushion** – the five-year financial plan approved by the IEC board of directors, which presents the liquidity sources and uses by the company, and according to which the bond issuing plan, that is also included in the five-year financial plan, is determined, do not reflect a ratio of 1.2, but a lower ratio.

**Normative average bond maturity of the IEC debt** – the Electricity Authority determined a normative average maturity that reflects the preference of mid-term structure of capital raising (7.1 years). The normative average maturity is short relative to the project life span and creates a disparity between the depreciation period on the asset and the debt repayment period, which increased the company's refinancing risks however reduces the capital costs and prevents tariff increase.






**The Stand Alone Credit Profile (SACP) of IEC** – the SACP (bb-) is lower by 4 notches than its general rating (BBB)<sup>7</sup> and belongs to the Below Investment Grade category. The rating indicates a high risk level in the absence of government support that the company receives.

**Risks to the continued improvement in the company's financial position** – major changes are occurring on the electricity sector, particularly concerning the government target of July 2020 to generate 30% of the electricity from renewable energies in 2030, entailing major investments, for a total of NIS 20 billion according to an initial estimate, by the IEC as the supplier of a vital service and as a monopoly in the transmission segment. The changes may affect the company's financial position and its ability to fulfill its goals as the supplier of a vital service.



**From 2012–2019 there was an improvement in the IEC financial position** expressed in a decrease of NIS 16 billion in its financial debt and improvements in the leverage level and in the company's liquidity. The raising terms of the Company were therefore improved, and its marginal interest for 2018 was 2.5%, the lowest since the company issued bonds for the first time.

## Key recommendations

-  It is recommended that IEC continue to act to improve its financial indicators, particularly the debt coverage ratios, the company's profitability and leverage, and at the same time examine its position from time to time compared to electricity companies worldwide. This examination may serve as an index for Company performance. It is further recommended that the company will base its continued activity to improve its financial resilience on efficiency and optimal management – and not by postponing vital activities in the electricity sector. Within this framework, it is recommended that the IEC examine the parameters that affect its stand-alone credit rating and continue to act towards its improvement, and reduce its dependence on government support.
-  It is recommended that the IEC formulate a coherent procedure for ongoing examination of the benefits from taking actions to reduce debt costs.
-  Holding a sufficient safety cushion reduces the Company's risks and allows it to maintain its credit rating. At the same time, holding a safety cushion in surplus entails costs. IEC should continue to hold a safety cushion that will balance these two considerations.

<sup>7</sup> Rating according to S&P. The credit rating by MOODY'S also shows that the baseline credit assessment (self-rating) (ba3) is 4 notches lower than the general rating (Baa2).





The three entities – the IEC, the Ministry of Energy and the Electricity Authority – should examine the disparities between the development plans for the transmission grid for 2013–2017 and the development plan approved for 2018–2022. They should examine the effect of postponing the various projects in the electricity system and what measures are required in order to compensate these differences.

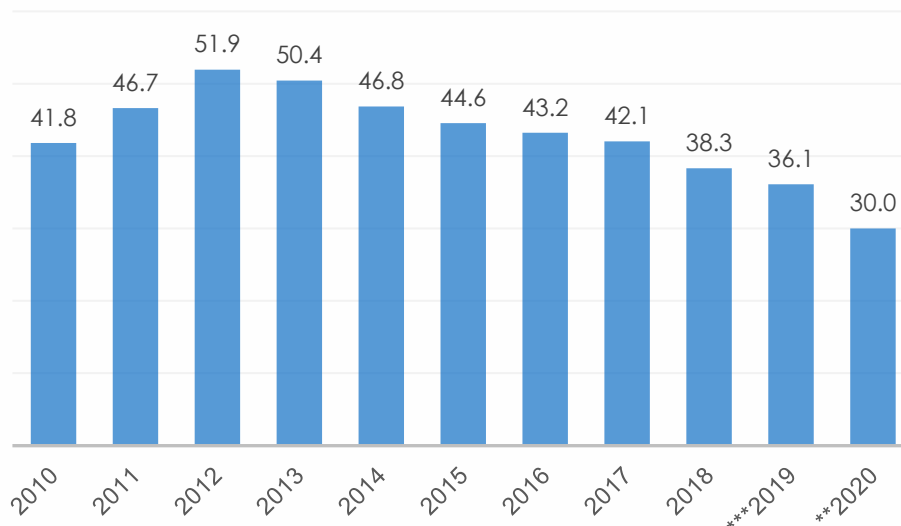


It is recommended that the Government Companies Authority together with the Capital Market Authority, the Bank of Israel and IEC, examine the barriers IEC is facing in the process of raising capital in Israel. The Electricity Authority and the Companies Authority should examine the IEC bond raising characteristics and the average bond duration so that the Company's bond raising model will be optimal.



The three entities – IEC, the Electricity Authority and the Ministry of Energy – should examine the challenges the electricity sector is facing in the coming years and their effect on the Company's financial position, and prepare for them alongside preserving IEC's financial resilience.



**The IEC's net financial debt, 2010–2020, in billions of NIS\***

The source: the IEC financial statements for 2011–2020 processed by the State Comptroller's office.

- \* The data for 2014–2019 are according to the IFRS (International Financial Reporting Standards), whereas the data for 2010–2013 are according to the Government Companies Regulations in adjusted NIS.
- \*\* The debt in 2020 includes surplus collection due to the sale of the Ramat Hovav power plant for a total of NIS 2.433 billion, that will be returned to electricity consumers.
- \*\*\* The debt in 2019 includes a surplus due to sale of the Alon Tavor power plant, which was returned to consumers in 2020.

## Summary

Over recent years the IEC debt decreased and its financial indicators improved. As a result, the company's capital raising conditions improved and its recent interest rates were at the lowest since the Company commenced raising capital. The improvement in the financial position of IEC over recent years and the reduction of its debt by 2017 are an amendment to the deterioration in its financial position following crises that the company faced, and a return to the situation prior to the fuel crisis and the global financial crisis of 2008 and 2009. In 2018 two agreements were signed between the IEC and the State, settlement of the assets and the reform on the electricity market, which lead to an additional improvement in the financial position of the IEC and to further reduction in the debt.





An analysis of the factors that brought about the debt reduction shows that most of the improvement is explained through disposable measures and not the result of routine measures taken in the company's ongoing operating activity. The operating actions taken to reduce the debt level contributed 16% of the debt decrease, which was done, among others, at the expense of investments in developing the electricity grid.

The audit also raised a concern that some of these requirements are not being resolved in the development plans for the coming years as well. At the same time, major changes occur in the electricity sector and these require extensive investments. This places the continued improvement in the company's financial situation at risk, and solutions will be required to carry out these changes without deteriorating the company's position. The IEC and government entities must provide the electricity economy requirements while at the same time maintaining the company's financial resilience.