



Report of the State Comptroller of Israel | July 2024

Ministry of Welfare and Social Affairs

Outsourcing of Social Services by the Ministry of Welfare and Social Affairs



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Background

An outsourced social service refers to an educational or treatment service purchased by the government and provided by external operators – private companies or non-profit organizations. These services are financed fully or partially by the government, which holds responsibility for their provision, regulation, and supervision (social procurement). The personal welfare services provided by the Ministry of Welfare and Social Affairs (Ministry of Welfare) encompass outsourced social services, categorized into two primary types: community services, where recipients do not reside at the service location (frameworks for at-risk children), and out-of-home services, provided in settings where recipients live permanently or temporarily outside their homes (residences for persons with disabilities). Local authorities are responsible for the provision of the community services, while the Ministry of Welfare is responsible for the provision of out-of-home services, including the selection of suppliers through social procurement tenders.

This report focuses on the procurement of out-of-home social services by the Ministry of Welfare within the Disability Administration, the Social and Personal Services Administration (SPSA), and the Rehabilitation, Support and Prevention Administration (RSPA). The significance of procurement in this domain is underscored by its financial implications; in 2022, the Ministry of Welfare expended about NIS 3.5 billion on outsourcing within these administrations, at about 36% of the Ministry's total budget for that year. The Ministry operates out-of-home services through selected bidders from tenders, with 254 external operators providing these outsourced welfare services in 2022.

Outsourcing welfare services presents several advantages, such as enhancing service quality, accessibility, and availability. However, it also poses challenges, including limitations on supervision and enforcement capabilities, as well as a lack of expertise in tender management. Furthermore, there exists a concern regarding "regulatory captivity", which refers to the significant dependence of regulators on service operators, potentially leading to biased decision-making favoring the operators and challenges in directing their activities. The extent to which these challenges manifest in the outsourcing of social services is heavily influenced by the actions of the Ministry of Welfare in its capacity as the regulator of social procurement.



Key Figures

NIS 3.5 billion

the scope of the Ministry of Welfare's annual expenditure in 2022 on the purchase of out-of-home social services from 254 operators in the Disabilities Administration, the Social and Personal Services Administration (SPSA), and the Rehabilitation, Support and Prevention Administration (RSPA)

2.5 times

the ratio between the average profitability rate in 2021 of private companies operating out-of-home frameworks for the Ministry of Welfare (9.7%) and the profitability rate set by the Ministry of Welfare (3.8%)

over 200%

the rate of accumulated surpluses (totaling NIS 393 million) among operators of frameworks classified as non-profit organizations, compared to the revenue turnover of 20% of them, most of whose revenue is predominantly derived from providing out-of-home services for the Ministry of Welfare

NIS 512 million

the estimated budget that the Ministry of Welfare pays to operators for unfilled positions

60%

the Ministry of Welfare tenders' rate of the procurement of social services in 2013–2022 in which every bid that passes the threshold conditions wins the tender, i.e. tenders in which there is no real competition (74 out of 128 tenders)

68%

the Ministry of Welfare bids' rate of tenders for the procurement of welfare services out of those that passed the threshold conditions that received the maximum score in category of recommendations (273 out of 401 bids)

89%


of the total payments for the provision of out-of-home welfare services, are paid by the Ministry of Welfare to operators with 17 years or more of experience in providing services to the Ministry of Welfare (about NIS 3.1 billion)

only 2–3 visits instead of 13–18

the median annual number of visits by inspectors in out-of-home settings compared to the recommendations of the Government Team for Improving the Provision of Outsourced Social Services from 2016





Audit Actions

 From January to October 2023, the State Comptroller's Office audited the Ministry of Welfare's actions regarding the procurement of outsourced welfare services. The audit focused on the structure of the out-of-home welfare services market, the rates for service provision, the supervision of service providers, and the planning of out-of-home welfare service offerings. The audit was carried out at the Disability Administration, the Social and Personal Services Administration (SPSA) and the Rehabilitation, Support and Prevention Administration (RSPA) within the Ministry of Welfare. Supplementary examinations were also conducted at the Competition Authority, the Prime Minister's Office, and the Chief Economist and Budget Divisions at the Ministry of Finance, as well as the Corporations Authority at the Ministry of Justice. It is important to note that the audit mainly examined the management of outsourced social procurement by the Ministry of Welfare and Social Affairs and did not assess the conduct or activities of the service providers.

To analyze the tender process for social procurement, and given the absence of a database from the Ministry of Welfare, the audit team collected tender documents and committee minutes discussing the bids submitted and electing the winning bids, for all social procurement tenders from 2013 to 2022. It extracted key data from these documents and converted them into quantitative variables, enabling analysis using advanced statistical tools such as regression analysis.

Key Findings


 **Redundancy (profit margins and surpluses) Among Operators of Out-of-Home Social Service Frameworks** – in 2022, the Ministry of Welfare procured out-of-home social services at about NIS 3.5 billion from 254 operators. "Redundancy" is identified among private operators when their income exceeds expenses, leading to profit margins, and among non-profit organizations when their surplus exceeds their revenue cycle. Aggregate data from the Chief Economist Division of the Ministry of Finance indicates that, among the 84 private companies providing social services to the Ministry of Welfare, the average profitability rate in 2021 is about 2.5 times higher than the intended profitability rate according to the level of revenues established by the Ministry of Welfare, resulting in an estimated difference of around NIS 106 million. When analyzing only those operators where at least 70% of their revenue cycle is derived from the provision of out-of-home services for the Ministry of Welfare, the profitability rate is found to be 2.3 times higher than the intended profitability rate, with an estimated difference of about NIS 88



million. Furthermore, an examination of the financial statements of all non-profit organizations, where at least half of the income is generated from out-of-home frameworks for the Ministry of Welfare (67 organizations) raises, among 38% of these organizations, surpluses exceeding 100% of their revenue cycle, at about NIS 725 million, while 20% have surpluses exceeding 200%, at about NIS 393 million.

📌 Dynamism Within the Welfare Services Market – the audit highlights the low level of dynamism within the welfare services market. Despite the high profitability rates that should encourage new entrants, the market remains predominantly controlled by operators with over 17 years of experience in providing services to the Ministry of Welfare. These operators constitute 76% of all framework operators (192 out of 254), at about 89% of total payments made in 2022 for out-of-home welfare services (about NIS 3.1 billion). This lack of operator turnover within existing frameworks, combined with limited entry of new operators, raises concerns regarding the concentration of power among these operators and the potential reliance on outdated treatment methods. The Government Team report from 2016 indicated that long-term engagements could lead to regulatory captivity regarding service operators and result in stagnation in service quality.


📌 Analysis of the Ministry of Welfare Tender Procedures for the Procurement of Social Services from External Operators


- **Competition in Tenders** – the outsourced social procurement tender market at the Ministry of Welfare, is unique as the service rates are predetermined and disclosed to all bidders, with competitive focus being placed solely on service quality rather than pricing. Within the tendering method employed in the provision of welfare services, competition among operators occurs at the tender stage. Analysis indicates that competition in the outsourced welfare services market is limited; about 60% of tenders from 2013 to 2022 (74 out of 128 tenders) exhibited no competition among the submitted proposals, with any qualifying proposal securing the tender. Consequently, the bidding mechanism fails to foster genuine competition in most instances.
- **Impact of Operator Tenure on Threshold Condition Compliance** – compliance with threshold conditions serves as an essential filter to determine whether bidders fulfill the requirements outlined in the tender. These conditions pertain to factors such as the operational structure, the workforce to be employed therein, and the bidder's financial stability. Bidders failing to meet all threshold conditions are disqualified from advancing to subsequent stages. Veterans in the bidding process (entities that have retained contracts with the Ministry of Welfare since 2005 or earlier) have a roughly 10 percentage point higher likelihood of meeting all threshold conditions compared to new bidders, who entered the market thereafter or have no engagements with the Ministry of Welfare. This indicates that



a fundamental cause of the stagnation in the social services market and the consolidation of power among established operators is the threshold conditions in tenders, which act as an entry barrier for new bidders. This is particularly evident in the administrative requirements that present a technical barrier, posing challenges for new entrants to meet.

- **Benchmarks for Evaluating Bids for Operating Out-of-Home Frameworks** – benchmarks serve as the main criteria for assessing the quality of bids for managing out-of-home frameworks. Findings indicate that 68% of bids meeting threshold conditions received the maximum score in recommendations, while 77% achieved the maximum score in terms of the bidder's experience. This suggests that these benchmarks are not effectively utilized as mechanisms for evaluating bid quality. Furthermore, the Ministry inspectors lack access to information regarding the contents of successful bids, and the Supervision and Control Division of the Ministry of Welfare is uninformed about the treatment plans and personnel proposed by winning bidders. Consequently, this division is unable to confirm that the services rendered align with the commitments made by operators. Ultimately, the established benchmarks intended to differentiate bid quality do not effectively bind winning bidders to deliver the promised service quality, leading to a scenario in which the tendering process, designed to stimulate competition on service quality, results in a competition merely "on paper". This framework benefits veteran bidders who are cognizant of tender process limitations and supervisory mechanisms, understanding that they are not necessarily obligated to fulfill their submissions in practice.

 **Involvement of the Competition Authority in the Regulation of Out-of-Home Welfare Services** – the Competition Authority, operating under the Economic Competition Law, 1988, is responsible for preserving and promoting free competition within the economy. The audit raised that the Competition Authority did not conduct a comprehensive examination of the welfare services market. Although a consultation took place between the Ministry of Welfare and the Competition Authority in February 2017 regarding specific tenders, this did not evolve into thorough cooperation or an in-depth analysis of market competition.

 **Determination of Out-of-Home Settings Rates** – to ensure adequate service levels for social service recipients, the Ministry of Welfare has set a uniform rate for social services by the operators, intended to reflect the anticipated costs associated with the inputs required per service recipient as per agreements with the Ministry. The audit raised that the rate mechanism is not differential and fails to align with the actual expense structure of operators, resulting in distortions, and creates disincentives for operators to fulfill all their contractual commitments to the Ministry of Welfare. For instance, the salary rates set within the rates system for nurses and doctors (NIS 11,000 and NIS 17,000, respectively) are significantly lower than their average salaries (NIS 22,000 and NIS 36,000, respectively) and are less than 40% of their median salary in




the civil service (NIS 19,000 and NIS 29,000, respectively). Additionally, the rent component in the rate is based on average costs, which may not appropriately reflect market conditions in central versus peripheral areas. The Ministry of Welfare has not amended the profitability rate, which has remained unchanged at 4% for over 25 years. In a high-interest rate environment, this static profitability rate does not incentivize new entrants to the social services market, as they are unaware that actual profitability is significantly higher and as they face the requirement of making new infrastructure investments at the outset of the contract.

Sanctions Against Operators for Insufficient Personnel Allocation – the enforcement procedure permits the Ministry of Welfare to offset payments from operators who fail to meet contractual obligations. Despite being aware of substantial personnel shortages among framework operators (notably a 42% deficit in social workers), the Ministry of Welfare refrains from applying the enforcement procedure concerning offsets. Consequently, of the estimated NIS 512 million disbursed annually, the Ministry pays operators for positions that remain unfilled, suggesting suspected damage to the public purse. The Ministry's failure to sanction the offsets and its ongoing payment for services not rendered reflects a disregard for compliance among contract violators, highlighting the Ministry's dependence on these operators. This situation not only undermines the integrity of public funds but also permits operators to deliver substandard services to recipients without facing consequences.

The Ministry of Welfare's Supervision of Out-of-Home Settings – the Ministry of Welfare has set a standard of 485 supervisory positions for out-of-home settings, yet currently employs only 453, leaving 32 positions unfilled. The supervisory role encompasses 50% control and enforcement tasks and 50% consulting tasks, yet many control components outlined in a 1950 government resolution are either absent or only partially fulfilled by the Ministry of Welfare. Thus, for example, there is inconsistency between the contract content and the inspectors' work, accompanied by an absence of monitoring for the rectification of deficiencies. Inspectors do not receive information regarding the successful bids or treatment plans associated with the frameworks in which they operate, nor do they verify that the services provided align with the commitments made by operators to enhance service quality. Moreover, the limited frequency of supervisory visits, averaging 2–3 per year, falls short of the government-recommended 13–18 visits annually, hindering the identification by the inspectors of service deficiencies, including issues related to shortages in treatment staff and substandard living conditions. Notably, between 2020 and 2022, the Ministry stopped placements in frameworks in about 40 instances of contractual violations by operators, relying solely on this sanction, without imposing financial penalties. Unlike some countries, for example the UK, where the Care Quality Commission (CQC) is an independent regulatory body involved only in supervision and enforcement, in Israel the district inspectors are tasked with both oversight and advisory roles.







 **The Ministry of Welfare's Financial Control over Out-of-Home Frameworks Operators** – the financial control exercised by the Ministry of Welfare over the operators of out-of-home frameworks is intended to ensure proper allocation of budgets in line with tender requirements, to provide optimal care for the residents, and to enhance financial transparency and supervision. However, the audit found that the Ministry does not effectively monitor the operators' financial practices. Beyond the initial tender phase, the Ministry does not require financial statements from operators incorporated as private companies, nor does it analyze the published statements of those incorporated as nonprofit organizations, even though they are published on the Ministry of Justice website. This inadequacy means that the Ministry does not routinely assess the financial stability of operators or identify warning signs of potential risks to their viability, if any, or to identify significant redundancies (profit margins and surpluses) among operators. Furthermore, it does not carry out a comprehensive financial audit to ascertain whether operators are utilizing the funds provided as agreed.



The Structures Threshold Conditions – a central component in the operation of out-of-home frameworks, mandates the existence of a structure suitable for the residence of service recipients. This threshold condition posed a significant barrier, particularly for new bidders who had not previously operated out-of-home frameworks. Until 2016, bidders were required to demonstrate ownership of a building as early as the first stage, as part of the threshold conditions. To facilitate this process for bidders and to expand competition, the Ministry of Welfare decided to suspend the requirement for proof of ownership of a building for a period exceeding one year. Following this policy change by the Ministry of Welfare in 2016, there was a marked decrease in the number of bidders disqualified for not meeting this threshold condition. The State Comptroller's Office commends the Ministry of Welfare's decision to ease this threshold condition, promoting the entry of new participants into the market.



Key Recommendations

-  **Analysis of the Bidding Process** – to enhance competition for the quality of social services, the Ministry of Welfare should increase the number of bids by implementing in tenders or in any other way, "nascent protection", which safeguards new bidders against the influence of dominant operators with longstanding market presence, thereby improving the level of competition in the initial phase. Additionally, it is recommended that it consider adjustments to the threshold conditions for bidders to enable participation by new entrants, thereby expanding competition in the subsequent phase and enabling effective ranking of bids based on quality. Furthermore, the Ministry should strengthen the interfaces between the selection phase of framework operators and the supervision and control phase, both by ensuring effective ranking of proposals based on accumulated experience with bidders and by notifying inspectors of winning proposals to monitor the fulfilment of operators' obligations.
-  **Benchmarks for Evaluating Bids for Out-of-Home Frameworks** – to guarantee that the benchmarks effectively function as a framework for the commitment of the winning bidders to service quality and promote competition in service quality during the bidding process, it is recommended that the Ministry of Welfare ensure that inspectors are informed about the content of the successful bids in the tender and verify that the operators comply with them. Furthermore, the Supervision and Control Division should receive information regarding the treatment plans and personnel proposed by the tender winners.
-  **Rates for the Provision of Out-of-Home Welfare Services** – to improve and refine the welfare services market, the Ministry of Welfare should reduce distortions in the existing rate mechanism and ensure that service operators deliver the full spectrum of required services. Rate structures should incorporate incentives for operators to retain treatment staff and mitigate burnout, impose offsets for absentee personnel, and periodically adjust profitability rates in line with changes in the economic environment, including fluctuations in the Bank of Israel interest rate or profitability of similar employment sectors.
-  **Supervision Scope over Out-of-Home Frameworks** – to ensure effective supervision of out-of-home frameworks, it is recommended that the Ministry of Welfare establish a standard for supervisory frequency tailored to the characteristics of various frameworks. This should inform the optimal number of frameworks each inspector oversees in accordance with established priorities and necessary staffing levels. Moreover, the Ministry should ensure that inspectors are well-informed of operators' obligations as per their agreements with the Ministry and the bids made during the tender process, imposing sanctions for repeated violations. Given the limited scope of the Ministry's supervision of out-of-home settings, coupled with the diverse responsibilities of inspectors, including consulting functions, it is recommended that the Ministry conduct an occupational analysis of the inspector position. This analysis should explore potential updates to the role, drawing



from successful models in other jurisdictions, such as the Care Quality Commission (CQC) in the United Kingdom, which focuses exclusively on control and enforcement.



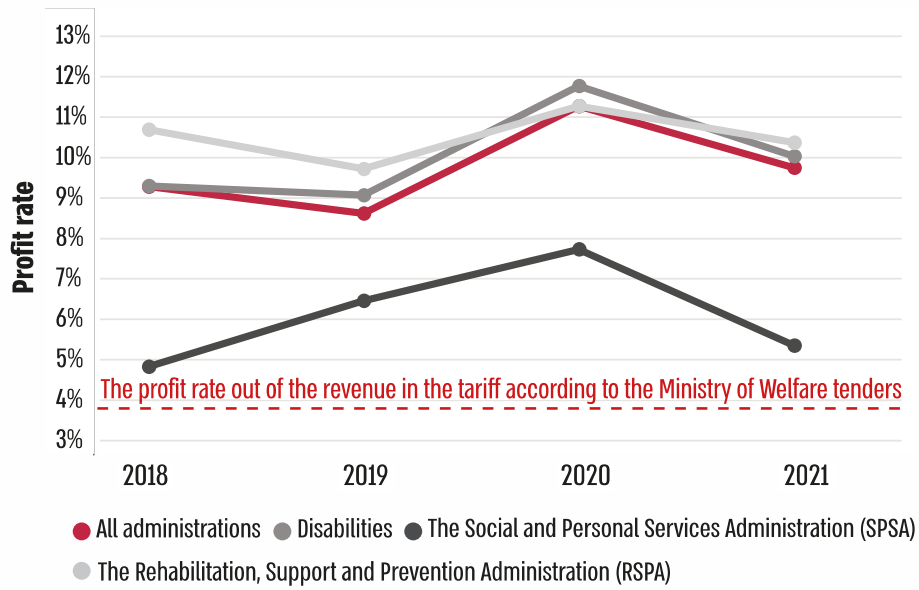
Financial Supervision of Out-of-Home Framework Operators – it is recommended that the Ministry of Welfare supervise the financial management of out-of-home framework operators. This should be achieved through the regular receipt of financial statements from operators and periodic in-depth assessments of their financial practices, conducted either in a sample-based manner or utilizing risk management principles.



Reevaluation of Welfare Service Provision Methods – globally, various recognized methods for providing social services, including welfare services, exist, which present differing levels of competition among providers. The specific combination of methods and the range of services encompassed within each are determined by the regulatory body, considering the nature of the service and the characteristics of its recipients. The "armored markets" approach grants licenses to non-profit organizations, resulting in limited competition. The "tenders combining price and quality" method bases competition on a combination of price and quality criteria. The "customer at the center" approach allocates the service budget directly to beneficiaries, allowing them to select their service providers. The "licensing" method offers recipients choice, emphasizing competition among suppliers as a key factor. Therefore, the pertinent government entities including the Ministry of Welfare, the Prime Minister's Office, the Competition Authority, and the Ministry of Finance should collaborate to form an inter-ministerial team tasked with evaluating service provision methods against global practices, and considering the diversity of services offered by the Ministry of Welfare and the characteristics of the service recipients. This includes factors such as the recipients' ability to make choices, the duration of assistance required by them, and their family environment.



The Average Pre-Tax Profit Rate of all Private Companies that Operated Out-of-Home Frameworks for the Ministry of Welfare in 2018–2021, Broken Down by Disabilities Administrations





Summary

The regulation of welfare services in Israel is governed by the Mandatory Tenders Law and its associated regulations, to ensure a sufficient number of bids to facilitate the selection of the most advantageous proposal and to promote fair and equitable competition. In 2022, the Ministry of Welfare allocated about 36% of its total budget, at about NIS 3.5 billion, towards the procurement of outsourced out-of-home social services. The current state of affairs, with respect to the characteristics of the social procurement market outsourced by the Ministry of Welfare, indicates signs of redundancy (profit margins and surpluses) among the operators of out-of-home frameworks. Audit findings indicate that the current tendering mechanism fails to foster genuine competition, as about 60% of tenders result in any compliant bid being awarded, and stifling dynamism in the social services market, which remains predominantly under the control of long-standing providers. A substantial 89% (NIS 3.1 billion) of payments for these services are directed to operators with 17 or more years of experience in providing services to the Ministry. This scenario stems from threshold conditions set within tenders that act as entry barriers for new bidders, including stringent administrative requirements that are challenging for newcomers, as well as benchmarks that do not necessarily correlate with the actual service quality provided, thus favoring established operators. The audit further reveals that the structure of the rate disbursed by the Ministry of Welfare to the operators of out-of-home frameworks does not align with their genuine expense structures, and the Ministry has not recouped over half a billion NIS for services reportedly unprovided. Additionally, there are challenges in the effective supervision of service quality.

Consequently, the tendering approach employed by the Ministry of Welfare for the management and procurement of outsourced welfare services is suboptimal, failing to achieve the intended competitive market structure that would enhance, in practice, service quality for its recipients.

To promote competition and improve the quality of social services in the short term, the Ministry of Welfare should strive to increase the number of bids in tenders by exploring the provision of "nascent protection" or alternative strategies. It is recommended to consider revising the threshold conditions for bidders to enhance competition without compromising bid quality, to inform inspectors of awarded bids, to mitigate distortions in the existing rate mechanism, and to offset the rate for insufficient staffing levels. Moreover, it is recommended that the Ministry conduct an occupation analysis for the inspector position and evaluate the necessity of updating the role in line with global models. From a strategic perspective regarding the long-term vision of the Ministry of Welfare's outsourced social procurement market, the Competition Authority, in cooperation with the Ministry of Finance, the Prime Minister's Office, and the Ministry of Welfare, should establish an inter-ministerial team to thoroughly assess the market for outsourced welfare services and identify optimal mechanisms to leverage competition advantages, while also considering alternative models for welfare service provision recognized internationally. This initiative to ensure the delivery



of quality services to recipients, particularly those belonging to the most vulnerable populations in Israeli society.