

The Auditor-General  
Audit Report No.15 2005–06  
Performance Audit

# **Administration of the R&D Start Program**

**Department of Industry, Tourism and Resources**

**Industry Research and Development Board**

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of Australia 2005

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Canberra ACT  
15 November 2005

Dear Mr President  
Dear Mr Speaker

The Australian National Audit Office has undertaken a performance audit in the Department of Industry, Tourism and Resources and Industry Research and Development Board in accordance with the authority contained in the *Auditor-General Act 1997*. Pursuant to Senate Standing Order 166 relating to the presentation of documents when the Senate is not sitting, I present the report of this audit and the accompanying brochure. The report is titled *Administration of the R&D Start Program*.

Following its presentation and receipt, the report will be placed on the Australian National Audit Office's Homepage—<http://www.anao.gov.au>.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Ian McPhee', with a long horizontal flourish extending to the left.

Ian McPhee  
Auditor-General

The Honourable the President of the Senate  
The Honourable the Speaker of the House of Representatives  
Parliament House  
Canberra ACT

## AUDITING FOR AUSTRALIA

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# Abbreviations/Glossary

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|                      |  |
|----------------------|--|
| ANAO                 | Australian National Audit Office.  |
| Applicant            | Company or research institution <sup>1</sup> applying for financial assistance.  |
| Application          | Formal request for financial assistance.   |
| AusIndustry          | A division of DITR responsible for delivering products, services and information that support industry, research and innovation.   |
| Commercial Ready     | The replacement program for R&D Start, the Biotechnology Innovation Fund and elements of the Innovation Access Program. Applications for grants under Commercial Ready commenced on 1 October 2004.  |
| CSM                  | Customer Service Manager.  |
| Deed of Agreement    | Contract between the Industry Research and Development Board and the grant recipient.  |
| DITR                 | Department of Industry, Tourism and Resources (referred to as the Department).   |
| Eligible expenditure | The Industry Research and Development Board defines the expenditure that qualifies as eligible for R&D Start-funded projects. It includes R&D labour expenditure, labour on-costs, administrative overheads, contract expenditure, certain expenditure on plant, prototype expenditure and certain miscellaneous expenditure such as market research related to the project. |
| FMA Act              | <i>Financial Management and Accountability Act 1997.</i>   |
| Grant recipient      | Applicant approved for grant financial assistance.   |
| Innovation Division  | A division of DITR responsible for providing policy advice to the Government on R&D Start.   |

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<sup>1</sup> Research institution is only applicable for R&D Start Graduate grants.

|                     |   |
|---------------------|---|
| IR&D Board          | The Industry Research and Development Board is responsible for the administration of R&D Start under provisions of the <i>Industry Research and Development Act 1986</i> . The Governor-General appoints members.   |
| KPI                 | Key Performance Indicator.  |
| R&D                 | Research and Development. R&D activities are systematic, investigative or experimental activities that involve innovation, technology transfer into Australia or technical risk.  |
| R&D Start           | A program that provides competitive grants and loans for Australian companies to undertake R&D, and its commercialisation. R&D Start closed to new applications in September 2004.  |
| Sectoral committees | Specialist committees that undertake technical and financial assessments of applications. There are three sectoral committees: Engineering and Manufacturing; Information Technology and Telecommunications; and Biological. Members of these committees are appointed by the Minister for Industry, Tourism and Resources. |



# Summary and Recommendations



# Summary

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## Background

This Government believes that innovation—developing skills, generating new ideas through research, and turning them into commercial success—is key to Australia’s future prosperity. Innovation is not only the province of new or high tech industries, but also essential to the future of many of our traditional sectors such as agriculture, manufacturing and mining.<sup>2</sup>

1. The Australian Government has a range of strategies designed to assist and build Australian innovation.<sup>3</sup> One of these is the R&D Start program, which provides Australian companies with grants and loans to undertake research and development (R&D) and for commercialisation of technical innovations. Since the program’s inception in 1996, some \$1.3 billion in grants have been approved.
2. The program supports projects that aim to develop new or improved products, processes, or services. Grants of up to \$15 million are available, though typically they range between \$100 000 and \$5 million. Loans are also available to meet some project costs.
3. The objectives of R&D Start are to:
  - (a) increase the number of projects involving R&D activities with a high commercial potential that are undertaken by companies;
  - (b) foster greater commercialisation of the outcomes of those projects;
  - (c) foster collaborative R&D activities in industry and between industry and research institutions;
  - (d) encourage successful innovation in small companies by supporting commercialisation of internationally competitive products, processes and services;
  - (e) increase the level of R&D activity in Australia that is commercialised in a manner that will benefit the Australian economy; and
  - (f) increase the level of R&D activities conducted that provides national benefit.<sup>4</sup>

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<sup>2</sup> John Howard The Hon, M.P., *Backing Australia’s Ability* (2000).

<sup>3</sup> These strategies include the 1998 Investing for Growth Statement, the 2001 Backing Australia’s Ability strategy, and the 2004 Backing Australia’s Ability—Building our Future through Science and Innovation strategy.

<sup>4</sup> Commonwealth of Australia, *R&D Start Program Directions No. 3 of 2002*, 28 November 2002, section 5.

4. The Industry Research and Development Board (the Board) has administrative responsibility for the program under the *Industry Research and Development Act 1986* (the Act).<sup>5</sup> Most administrative responsibilities have been delegated to sectoral committees<sup>6</sup> or to AusIndustry, a division of the Department of Industry, Tourism and Resources.

5. In 2004, the R&D Start program was merged with other innovation programs to form the Commercial Ready program. The objectives and delivery strategies for Commercial Ready are similar to those of R&D Start, but no loans are offered under the new program. Applications for grants under the Commercial Ready program commenced on 1 October 2004.

6. Administration of existing R&D Start grants will continue for up to 10 years.

## This audit

7. The objective of the audit was to assess the Commonwealth's administration of the grants component of the R&D Start program. Lessons for the new Commercial Ready program have been identified in the audit. Accordingly, recommendations arising from this audit are directed, when appropriate, to the Commercial Ready program.

8. As most financial assistance is in the form of grants, the loans component of the program was excluded from the audit.

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<sup>5</sup> The Governor-General has appointed members with relevant industry, management and academic backgrounds to the Board.

<sup>6</sup> There are three sectoral committees: Biological; Engineering and Manufacturing; and Information Technology and Telecommunications.

# Key Findings

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## Aspects of program governance (Chapter 2)

9. Under the Act and ministerial directions, the Board is the approver of spending proposals. The Secretary of the Department is accountable, under the *Financial Management and Accountability Act 1997*, for the proper expenditure of public money appropriated to the Department.
10. The Board has delegated most of the administrative activities for R&D Start to the three sectoral committees and AusIndustry. Documents outlining the delegations and the Board's policies and procedures provide a clear articulation of, and framework for, program administration.
11. The Department did not have procedures in place to be assured that the Board, by approving spending proposals, had not over committed the program's annual allocation. This weakness resulted in the program over committing its allocation by \$60 million in 2001–02. The shortfall was met by a \$20 million reallocation of funds from other innovation programs, and an advance of \$40 million from future appropriations for R&D Start.
12. Because of the over commitment of program funds, the Board ceased approving grants from January 2002. The program was formally suspended in May 2002. It was reopened in November 2002. Prior to its reopening, the Board and the Department put in place new financial management arrangements to prevent a reoccurrence of such over commitments. The key corrective action was the delegation of responsibility for the financial control of R&D Start funds to a senior executive officer of AusIndustry. However, the delegation did not resolve the overlap in the legislated financial management accountability for R&D Start between the Board and the Department.
13. The legislative provisions relating to the Board's financial management responsibilities were removed from the Act and ministerial directions prior to the commencement of the new Commercial Ready program in October 2004. Under the revised legislative arrangements, DITR is responsible for the administration of Commercial Ready.
14. The program's performance measurement framework has some limitations that affect its usefulness in measuring the achievement of objectives and outcomes. For example, the relevance of some Key Performance Indicators to measure program outcomes is not clear. Also, specific targets have not been defined for Key Performance Indicators, to enable performance to be assessed.
15. Prior to 2004, two independent evaluations were conducted to assess the program's effectiveness. In 2004, AusIndustry commenced biannual surveys to collect information on a sub-set of the program's outcome measures

and Key Performance Indicators. A low response rate to the first two biannual surveys undermined the reliability of the initial results, as the results could not be readily extrapolated to the target grant population.

16. Notwithstanding the limitations, the survey results suggest that participation in R&D Start has produced positive results for grant recipients and the wider community.

17. The Board and committee members are drawn largely from the private sector. This provides commercial and technical expertise to inform decisions. Inevitably, this means that many of these members have links to industry, creating a need to manage the risk of perceived or actual conflicts of interest.

18. For the Board and its committees, the Act requires disclosure of direct or indirect pecuniary interest by a member in a matter being considered, or about to be considered. The ANAO found that the Board's Conflict of Interest and Statement of Private Interests policies are in accordance with recognised better practice principles, and meet the requirements of the Act. The ANAO observed the policies working well in practice.

### **Access to the program (Chapter 3)**

19. R&D Start, and its successor, Commercial Ready, have been promoted as part of AusIndustry's suite of innovation programs. Market surveys are conducted to assess the effectiveness of the awareness raising activities, but these are not conducted regularly. The most recent survey of the target audience, conducted in 2002, indicated that promotional and marketing activities are effective at raising awareness. Some 71 per cent of businesses and 67 per cent of professional bodies and industry groups were aware of the program.

20. As professional bodies and industry groups are a cost effective way to increase the awareness of potential applicants, AusIndustry has targeted them in its awareness raising activities since 2002. However, it has not measured the effectiveness of its increased targeting. This is important to evaluate and inform the development of such strategies.

21. AusIndustry allocates a Customer Service Manager to a potential applicant so as to provide a single point of contact, simplifying access to information and advice. The ANAO found that AusIndustry places a high priority on matching the Customer Service Manager's skills with the potential applicant's project or, if possible, allocating a Customer Service Manager to a potential applicant with whom they have worked previously.

22. Approximately 80 per cent of respondents to the 2003 and 2004 Customer Satisfaction Surveys<sup>7</sup> agreed that AusIndustry staff provided advice that was clear, consistent and comprehensive.

## Processing of applications (Chapter 4)

23. The decision to approve or reject an R&D Start application was made in four stages.

24. Firstly, AusIndustry confirmed that the application met the program's eligibility requirements. Where eligibility could not be established clearly by AusIndustry (for example, the ability of the applicant to meet its share of project costs), the application was sent to the relevant committee to determine eligibility. AusIndustry implemented several initiatives to improve the ability of its staff to determine eligibility but has not measured the effectiveness of these initiatives.

25. At the second stage, AusIndustry assessed the strengths and weaknesses of each eligible application, and provided the relevant committee with its assessment, as well as a recommendation on whether the application should be supported. A merit rating between 1 (low merit) and 6 (very high merit) was assigned to each criterion, and the individual merit ratings were then summed to give a total rating score that was used to determine competitiveness.

26. In the third stage, having regard to AusIndustry's ratings, a committee assessed the project, and recommended to the Financial Delegate whether the project was sufficiently competitive to justify financial assistance. In 2003–04, 80 per cent of AusIndustry's assessments of the competitiveness of applications were the same as those of the relevant committee. In 20 per cent of cases, committees recommended the application be rejected, whereas AusIndustry recommended it be supported.

27. AusIndustry had no structured approach to analysing the reasons for the different recommendations, so as to identify improvements that could be made to the quality of advice to committees. The ANAO found that, in 22 per cent of cases, AusIndustry had recommended supporting the application where the total rating score was high, but it had given one merit criterion a low rating. Committees had not supported any of these applications.

28. A common process for appraising applications accords with grant administration better practice. Although appraisal procedures had only been

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<sup>7</sup> AusIndustry collects information from successful and unsuccessful applicants in its Customer Satisfaction Surveys.

documented for one of the four committees, each committee developed substantially the same procedures for assessing an application's level of competitiveness.

29. However, in 2003–04, committees used different minimum total rating scores to recommend support for applications. The different levels were not based on a risk, merit based, or other rationale, nor was the reason for the different levels documented. Although the observed differences in the ratings were small, the lack of a rationale for the difference undermines transparency and risks claims of bias. Without adequate controls, there is a risk that the difference will increase over time, resulting in applications from different industry sectors being subjected to quite different standards of competitiveness without a clear reason why.

30. The Board and AusIndustry did not undertake regular comparative analyses of the proportions of applications supported by committees, or the extent to which any differences in these proportions were reflected in the subsequent commercial success of projects.

31. The ANAO found that the proportion of applications supported by the Information Technology and Telecommunications Committee was lower than other committees. AusIndustry advised that this is likely to be a result of the committee receiving a higher rate of less meritorious applications than other committees.

32. On the other hand, small grant applications had a relatively high rate of support (by the AusIndustry R&D Start Committee). Available data on project outcomes indicate that these smaller grant projects also have a higher rate of subsequent commercial success.

33. The final stage in the processing of applications was the approval or rejection of the application by the Financial Delegate. Prior to approval, the Financial Delegate confirmed that the recommendation was consistent with the program's objectives and there were sufficient uncommitted funds to meet the new financial obligations. For the applications examined by the ANAO, the Financial Delegate approved grants in accordance with the financial management delegation.

## **Contractual arrangements (Chapter 5)**

34. The Board, on behalf of the Commonwealth, established a formal contractual arrangement with the successful applicant(s) before grant payments commenced. This contract is called a Deed of Agreement (the Agreement).

35. AusIndustry used a template document to produce Agreements. The ANAO found that the Agreement provides sufficient information to allow



AusIndustry to determine that the grant is used for the agreed purpose, and that grant payments are made according to progress of the project. The Agreements also clearly articulate the requirements that must be met by grant recipients for payments to be made.

36. The ANAO found that most terms and conditions, such as project start and finish dates, timings of milestones and annual expenditure profile, were accurately reflected in the Agreements examined. Some due dates for progress reports were inconsistent with the program's reporting guidelines.

37. These Agreements were also signed in accordance with the Board's requirements.

## Compliance with contractual arrangements (Chapter 6)

38. The grant recipient reports to AusIndustry each quarter on the project's progress. If progress is assessed as satisfactory, AusIndustry makes quarterly payments to the grant recipient.

39. The proportion of progress reports submitted to AusIndustry by the due date has almost doubled from 31 per cent in 2001–02 to 60 per cent in 2004–05. Overdue reports have little impact on the program in the short term as AusIndustry does not make a grant payment without a report having been received and assessed. No penalties have been imposed on a grant recipient for late reporting.

40. Assessment of progress reports can be by a desk audit of the claims made in the report or by visiting the grant recipient. The targets for site visits are inconsistent across different components of AusIndustry's risk management strategy.

41. AusIndustry did not achieve its targets for the number of visits undertaken. In 2004–05, only 25 per cent of high-risk projects were visited, against a target of 100 per cent. Approximately 60 per cent of **all** projects were visited in 2004–05, also against a target of 100 per cent.

42. There is discretion to conduct end-of-project visits for low-risk projects. However, AusIndustry does not monitor the use of that discretion, despite this being the last opportunity for AusIndustry to assure itself that projects achieved the outcomes in accordance with Agreements. Over the period 2001–02 to 2004–05, AusIndustry visited approximately half of the projects at their completion.

43. Once progress has been assessed as satisfactory, AusIndustry calculates the grant payment. The ANAO found that the steps in calculating the level of the payment are adequately defined in the Procedures Manual. Proformas and checklists are used to ensure all steps are undertaken.

44. The payments examined by the ANAO were made according to the approved amounts set out in Agreements, or had been appropriately varied. Also, payment calculations were generally appropriately checked and authorised, and retained on the project file, providing an audit trail.

45. AusIndustry does not confirm that project expenditures claimed in quarterly progress reports comply with the program's eligible expenditure guidelines. Instead, it relies on an annual audit certificate issued by an independent auditor appointed by the grant recipient.

46. As part of its compliance management strategy, AusIndustry is planning to implement an audit program that aims to substantiate the veracity of independent audit certificates submitted by the grant recipients. AusIndustry planned to conduct 20 audits as a pilot in 2004–05, but only conducted nine. AusIndustry advised in response to the draft report that, following an analysis of the results of the nine completed audits, it has set a target of 12 substantiation audits for 2005–06.

## Overall audit conclusion

47. The ANAO concluded that the delivery of the R&D Start program is generally well managed by AusIndustry. Improvements in some areas would further strengthen the framework, improve the efficiency of the delivery of grant financial assistance, and provide greater transparency to stakeholders.

48. The key governance arrangements are well established and roles and responsibilities of the Industry Research and Development Board, its committees, Innovation Division and AusIndustry are clearly articulated.

49. However, prior to 2002, arrangements for addressing financial management accountabilities were insufficiently clear, leading to an over commitment of funds and the suspension of the program. New financial management arrangements were introduced prior to the reopening of the program. These arrangements addressed the weakness in the previous system relating to lack of clarity of financial management accountabilities.

50. Sound procedures are in place to manage the potential for perceived and actual conflict of interest.

51. The Innovation Division-AusIndustry Business Partnership Agreement defines the program's performance measurement framework. However, there are limitations in the framework that affect its usefulness, including the relevance of some Key Performance Indicators and the lack of specific targets that enable performance to be assessed. In addition, surveys conducted to collect outcome information have low response rates. Addressing these gaps would provide AusIndustry and the Board with better information against

which to assess program performance, improve public reporting, and properly evaluate the program.

52. Based on the available performance information, survey findings suggest that the program has had positive impacts on companies that have received R&D Start grants. Also, an independent evaluation conducted in 2003 estimated that the national economic benefits resulting from the program have been of the order of \$4.50 for every R&D Start dollar.

53. The procedures for appraising applications generally followed better practice. However, committees selecting applicants for financial assistance used different minimum rating scores, creating relative differences in the level of competitiveness required to receive financial assistance.

54. The contractual agreement between AusIndustry and grant recipients provides a sound accountability framework for the management of grants.

55. AusIndustry's approach to monitoring compliance against the obligations in the Agreement is supported by detailed standard operating procedures, which are reasonably well documented and implemented. Improvements are still required to ensure grant recipients adhere to the due dates of their progress reports, so as to minimise the risk that the program's budget allocation will be underspent.

56. Applicants are generally satisfied with the quality and timeliness of the service provided by AusIndustry.

57. Lessons learned from administering R&D Start have been incorporated in administrative processes, either for R&D Start, or for the new Commercial Ready program.

## Recommendations and responses

58. The ANAO made six recommendations aimed at strengthening the administration of R&D grants under the R&D Start and Commercial Ready programs. All recommendations were agreed.

59. The Department provided the following summary comments:

DITR is pleased with the ANAO's conclusion "that the delivery of the R&D Start program is generally well managed by AusIndustry" (paragraph 47). In addition, the ANAO has found that lessons learned from administering R&D Start have not only been used to improve the administration of R&D Start, but have also been adopted in the new Commercial Ready program.

DITR agrees with the ANAO's recommendations and acknowledge their potential impact in strengthening or further improving the delivery of the program. However, DITR notes that in any assessment process involving a range of views, there will always be some degree of disparity in overall scores

reflecting individual judgments, and there is a specific role for the committees who have the technical and industry expertise in the assessment process.

**60.** The Industry Research and Development Board provided the following summary comments:

The Board is pleased with the ANAO's conclusion that the delivery of the R&D Start program is generally well managed by AusIndustry and the key governance arrangements between the Board, its committees and DITR are well established and clearly articulated. The Board is assured by the ANAO's findings that its conflict of interest policies are "in accordance with recognised better practice principles" and sound procedures were found to be in place to manage conflicts of interest.

# Recommendations

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## Recommendation No.1 Paragraph 2.40

The ANAO recommends that AusIndustry and the Innovation Division of DITR strengthen the performance management framework for R&D Start and Commercial Ready by:

- improving the relevance of KPIs for measuring the achievement of program objectives and outcomes; and
- setting targets for KPIs, so that performance can be assessed.

*DITR and the IR&D Board Responses: Agreed.*

## Recommendation No.2 Paragraph 2.51

The ANAO recommends that AusIndustry improve information available to evaluate program outcomes by:

- regularly analysing the non-response rate for biannual surveys of grant recipients to identify the nature of the non-response, and any associated bias;
- including this information in any reports of the survey data; and
- implementing strategies to encourage grant recipients to supply information requested by AusIndustry, in accordance with their grant obligations.

*DITR and the IR&D Board Responses: Agreed.*

## Recommendation No.3 Paragraph 4.18

The ANAO recommends that AusIndustry undertake regular structured analysis of the reasons for any differences between AusIndustry and committee recommendations for the new Commercial Ready program, in order to develop strategies to improve the quality of advice given to committees.

*DITR and the IR&D Board Responses: Agreed.*

**Recommendation  
No.4  
Paragraph 4.30**

The ANAO recommends that, for transparency and accountability to stakeholders, committees apply consistent minimum total rating scores to Commercial Ready applications, or a rationale for any differences be documented.

*DITR and the IR&D Board Responses: Agreed.*

**Recommendation  
No.5  
Paragraph 4.43**

The ANAO recommends that AusIndustry strengthen quality assurance by:

- evaluating committee recommendations for Commercial Ready grant applications to identify reasons for differing rates of approval across committees; and
- assessing the extent to which any differences are reflected in the subsequent commercial success of projects.

*DITR and the IR&D Board Responses: Agreed.*

**Recommendation  
No.6  
Paragraph 6.26**

The ANAO recommends that AusIndustry set clear and consistent site visit targets for Commercial Ready and R&D Start projects, and where discretion for conducting visits is allowed, monitor the use of such discretion in order to inform decisions about the targets.

*DITR and the IR&D Board Responses: Agreed.*

# **Audit Findings and Conclusions**





# 1. Introduction

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## Background

**1.1** Business innovation, through the development of commercial products, processes and services, is a key driver of domestic productivity, international competitiveness and economic growth. The R&D Start program, one of a suite of innovation support programs,<sup>8</sup> contributes to increasing the level of business innovation through the provision of competitive grants and loans for Australian companies to undertake research and development (R&D) and its commercialisation.<sup>9</sup>

**1.2** Since the program's inception in 1996, approximately 1 300 R&D grants valued at nearly \$1.3 billion have been approved. In addition, concessional loans of approximately \$73 million have been provided.

**1.3** In the 2004 Federal budget, the government announced that R&D Start, the Biotechnology Innovation Fund and elements of the Innovation Access Program would be merged to form the Commercial Ready program.<sup>10</sup>

**1.4** The Commercial Ready program is expected to improve access to government assistance by the consolidation of the three programs, which will reduce industry compliance costs through a streamlined application process. Also, the type of activities eligible for grant support will now include proof of concept and early stage commercialisation activities. This is expected to improve commercialisation outcomes for small and medium-sized enterprises.

**1.5** R&D Start closed to new applications in September 2004. Existing grants and loans will continue to be administered for up to 10 years. Grant payments could continue for up to five years.<sup>11</sup> In addition, the reporting of commercialisation outcomes for R&D Start-supported projects will be required for a further five years, following completion of the grant.

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<sup>8</sup> This includes the Commercialising Emerging Technologies (COMET) program and the Innovation Access Program.

<sup>9</sup> Research and development activities are systematic, investigative or experimental activities that involve innovation, technology transfer into Australia or technical risk. (R&D Start Program, *Customer Information Booklet*, section 2.2)

<sup>10</sup> New funding for the Commercial Ready program, in addition to funding for existing programs, is \$1 billion for the period 2004–05 to 2010–11. Department of Industry, Tourism and Resources, *Portfolio Budget Statements, 2004–05*, p. 56.

<sup>11</sup> Initial Core Start and Start Plus grant approvals may be for up to three years. However, variations to a project's duration may extend the term of the grant up to a maximum of five years.

1.6 Applications for grants under Commercial Ready commenced on 1 October 2004. Administrative procedures for Commercial Ready are similar to those used to administer R&D Start.

## Types of financial assistance under R&D Start

1.7 R&D Start consists of five elements. These are described in Figure 1.1.

**Figure 1.1**

### Elements of the R&D Start program

| Program element    | Grant/loan | Eligible companies  | Financial assistance  |
|--------------------|------------|---|---|
| Core Start         | Grant      | Annual turnover of less than \$50 million in each of the last three fiscal years. | Up to 50% of eligible project costs.  |
| Start Plus         | Grant      | Annual turnover of \$50 million or more in any of the last three fiscal years.    | Up to 20% of eligible project costs.  |
| Start Graduate     | Grant      | Annual turnover of less than \$50 million in each of the last three fiscal years. | In collaboration with a research institution, grant up to \$100 000 to engage a graduate on a specific R&D project. |
| Start Premium      | Loan       | A 'top-up' loan available to recipients of Core Start or Start Plus.              | A maximum of grant plus loan to a value of 56.25% of eligible project costs.  |
| Concessional loans | Loan       | Small companies (less than 100 staff).  | Up to 50% of eligible commercialisation costs.  |

Source: Industry Research and Development Board

1.8 Most R&D Start financial assistance provided was in the form of grants, typically ranging in value between \$100 000 and \$5 million. However, grants up to \$15 million were available. Figure 1.2 presents a breakdown of the financial assistance provided over the period 2001–02 to 2004–05.

**Figure 1.2****R&D Start approvals, 2001–02 to 2004–05**

| Program element               | Applications approved |              |           |             |            |              |            |              |
|-------------------------------|-----------------------|--------------|-----------|-------------|------------|--------------|------------|--------------|
|                               | 2001–02               |              | 2002–03   |             | 2003–04    |              | 2004–05    |              |
|                               | no.                   | \$m          | no.       | \$m         | no.        | \$m          | no.        | \$m          |
| Core Start                    | 106                   | 107.6        | 79        | 80.7        | 130        | 154.2        | 100        | 109.5        |
| Core Start, plus Premium loan | -                     | -            | 1         | 2.4         | 1          | 0.8          | -          | -            |
| Start Plus                    | 1                     | 0.3          | -         | -           | -          | -            | 2          | 5.5          |
| Start Plus, plus Premium loan | 1                     | 2.1          | -         | -           | 1          | 9.4          | -          | -            |
| Start Graduate                | 7                     | 0.6          | 6         | 0.6         | 10         | 1.0          | 9          | 0.9          |
| Concessional loans            | 7                     | 3.1          | 8         | 8.4         | 15         | 11.2         | 4          | 5.8          |
| <b>Total</b>                  | <b>122</b>            | <b>113.7</b> | <b>94</b> | <b>92.1</b> | <b>157</b> | <b>176.6</b> | <b>115</b> | <b>121.7</b> |

Source: Industry Research and Development Board Annual Reports and AusIndustry

## Legislative and administrative framework

**1.9** The Industry Research and Development Board<sup>12</sup> (the Board) is responsible for the administration of R&D Start under provisions of the *Industry Research and Development Act 1986* (the Act), and directions issued by the Minister for Industry, Tourism and Resources.<sup>13</sup>

**1.10** Three sectoral committees,<sup>14</sup> appointed by the Minister, assist the Board to administer the program. The committees undertake technical and financial assessments of applications and recommend to the Board whether applications should receive financial assistance. The Board delegates its authority to approve financial assistance to a Financial Delegate in AusIndustry.

**1.11** AusIndustry, a division of the Department of Industry, Tourism and Resources (DITR), assists the Board to deliver the program. It provides secretariat support to the Board and the committees, processes applications, calculates and approves grant payments, and manages the program's annual budget allocation of funds. In addition, the Executive General Manager of AusIndustry assesses applications for grants less than \$250 000 under a delegation from the Board. The Executive General Manager established a

<sup>12</sup> The Board comprises private sector and academic members with expertise and experience in R&D and commercialisation. Members are appointed by the Governor-General for a period up to three years.

<sup>13</sup> Commonwealth of Australia, *R&D Start Program Directions No. 3 of 2002*, 28 November 2002.

<sup>14</sup> Biological; Engineering and Manufacturing; and Information Technology and Telecommunications Committees.

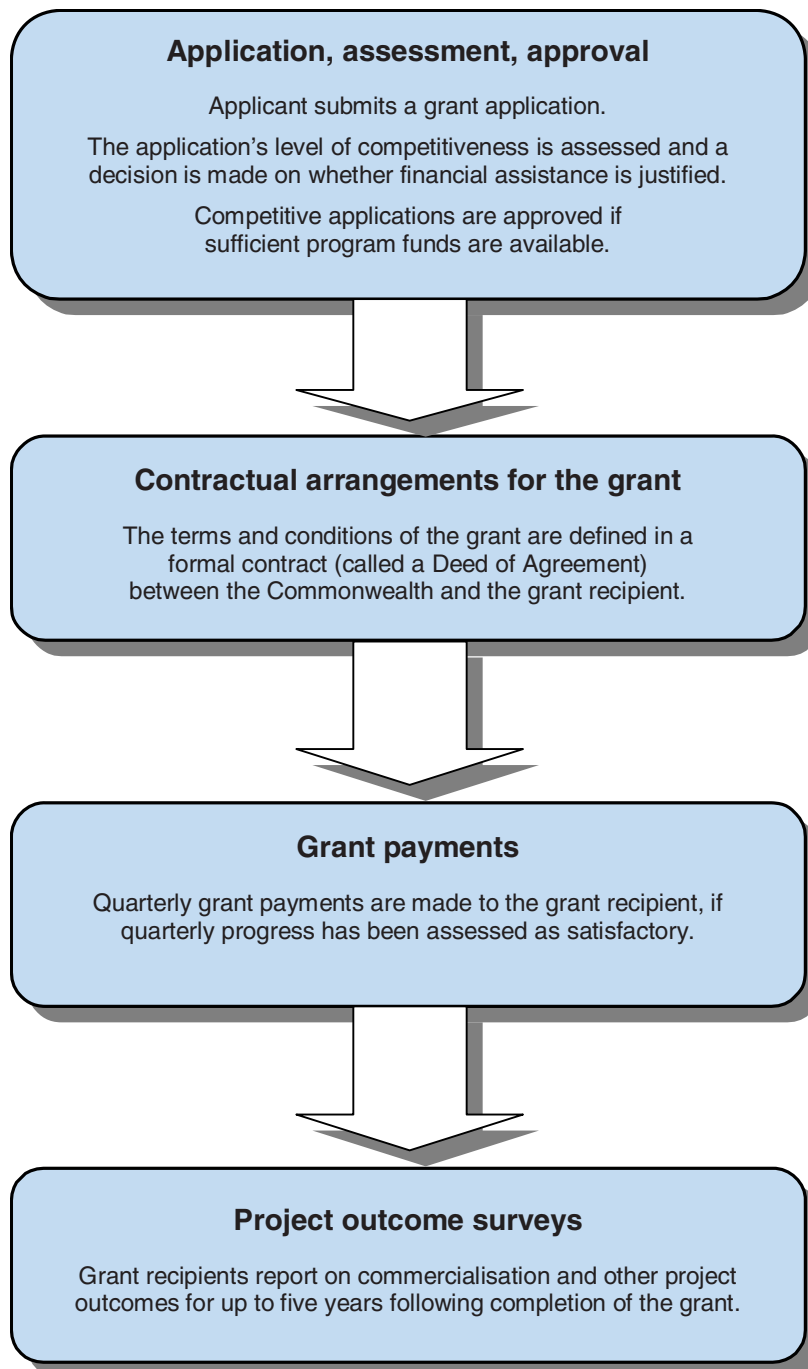
committee of senior AusIndustry officials to assist in the assessment process. This committee was called the AusIndustry R&D Start Committee.<sup>15</sup>

## Grant administration process

**1.12** The major stages of the grant administration process are set out in Figure 1.3. Details on each stage, including the roles and responsibilities of the Board, committees, AusIndustry and grant recipients are discussed throughout the report.

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<sup>15</sup> For ease of reference, the ANAO refers to the three sectoral committees and the AusIndustry R&D Start Committee as 'the committees'.

**Figure 1.3****R&D Start grant administration process**

Source: ANAO

## This audit

### Audit objective

1.13 The objective of the audit was to assess the Commonwealth's administration of the grants component of the R&D Start program.

1.14 The loans component of the program was excluded from the audit as it was small and the new Commercial Ready program does not have a loan component.

### Audit methodology

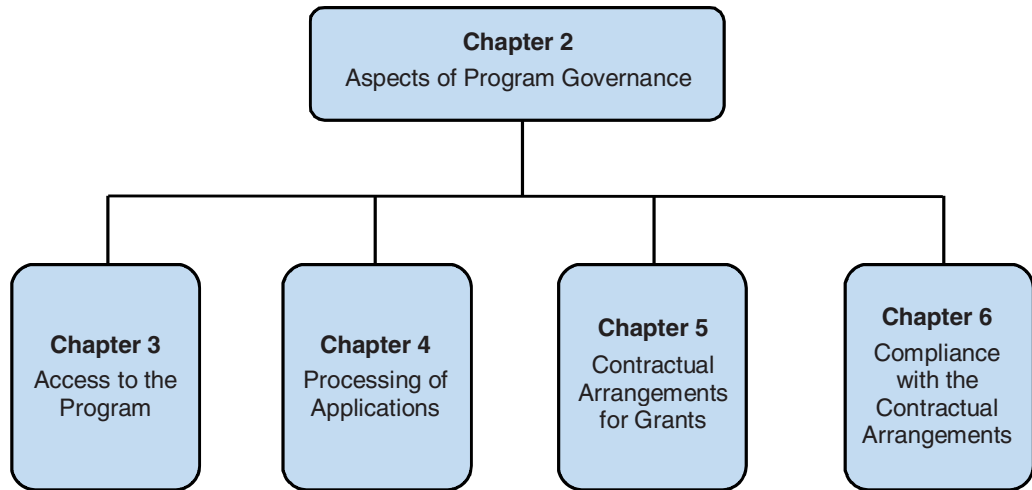
1.15 ANAO fieldwork included:

- interviews of staff in AusIndustry, including State and Territory offices, and other divisions of DITR;
- interviews of members of the committees, and observations of the decision making procedures of two committees;
- a review of Board policies, customer guidance material, and AusIndustry Procedures Manual used to administer the program;
- a review of the results of Customer Satisfaction Surveys;
- an analysis of project files and grant management information systems relating to 31 case study projects; and
- discussions with successful and unsuccessful applicants and stakeholders.

1.16 The audit was conducted in accordance with ANAO auditing standards and cost \$425 000.

### Structure of this report

1.17 The structure of this report is outlined in Figure 1.4.

**Figure 1.4****Structure of the report**

## 2. Aspects of Program Governance

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*This chapter examines some elements of the program governance framework relevant to R&D Start.*

### Roles and responsibilities

**2.1** Three key partners—the Industry Research and Development Board (the Board), AusIndustry and the Innovation Division of DITR—share responsibility for the administration of R&D Start. Clear roles, responsibilities and accountabilities are an important aspect of program governance, particularly where responsibilities for a program are shared.

### The Industry Research and Development Board

**2.2** The Board's roles and responsibilities in the administration of R&D Start are stated in ministerial directions issued under the Act.<sup>16</sup> The ministerial directions specify that the Board must administer the program by: considering applications and selecting applicants for financial assistance; entering into agreements with successful applicants; authorising payments for financial assistance to be made by the Commonwealth; and monitoring and evaluating projects for which assistance is provided.

**2.3** The ministerial directions also provide the Board with specific guidance on how the program is to be administered, including:

- the maximum amount that may be approved for the different types of financial assistance offered under R&D Start;
- eligibility requirements for the applicant and the project; and
- the merit criteria to be used to assess an application's level of competitiveness.

**2.4** The ANAO found that the legislative framework for the program clearly defines the Board's roles and responsibilities in the administration of R&D Start.

**2.5** However, prior to 2002, there was a lack of clarity regarding the accountability for the financial management of R&D Start. This is discussed below.

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<sup>16</sup> Commonwealth of Australia, *R&D Start Program Directions No. 3 of 2002*, 28 November 2002, section 7.



### *Administrative responsibilities*

**2.6** The Board delegates most of its administrative responsibilities to the three sectoral committees<sup>17</sup> and AusIndustry. To assist delegates to exercise their powers, the Board has issued a number of policies and procedures outlining its requirements for the administration of the program.

**2.7** The ANAO found that, overall, the delegations and the Board's policies provide a clear articulation of, and framework for, the program's administration.

### *Accountability for the management of program funds*

**2.8** Under the Act and the ministerial directions, the Board is the approver of spending proposals for R&D Start. Under government regulations,<sup>18</sup> an approver of spending proposals must not approve a proposal to spend public money unless the approver is satisfied that the proposed expenditure is in accordance with the policies of the Commonwealth, and will make efficient and effective use of public money.

**2.9** In addition, under the *Financial Management and Accountability Act 1997*, the Secretary of DITR is accountable for the proper expenditure of public money appropriated to the Department. In meeting these responsibilities, it is good practice for the Department to monitor R&D Start expenditure to ensure it is in accordance with the program's annual budget allocation.

**2.10** The Department did not have procedures in place to be assured that the Board, by approving spending proposals, had not over committed the program's annual allocation. This weakness resulted in the program over committing its allocation in 2001–02 (see paragraphs 2.22 to 2.25).

**2.11** Clarity of accountability was enhanced in 2002 when the Board delegated, to an AusIndustry senior executive officer, the authority to approve R&D Start grants. This delegation provided an appropriate mechanism for the Secretary of DITR to monitor the commitment of the program's funds. However, the delegation did not resolve the overlap in the legislated financial management accountability for R&D Start between the Board and the Department.

**2.12** The legislative provisions relating to the Board's financial management responsibilities were removed from the Act<sup>19</sup> and ministerial directions prior to the commencement of the new Commercial Ready program in October 2004.

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<sup>17</sup> Biological; Engineering and Manufacturing; and Information Technology and Telecommunications Committees.

<sup>18</sup> Financial Management and Accountability Regulations 1997, Regulation 9.

<sup>19</sup> See *Industry Research and Development Amendment Act 2004*, No. 15, 2004. The amendments came into effect on 11 September 2004.

Under the revised legislative arrangements, DITR is responsible for the administration of Commercial Ready,<sup>20</sup> while the Board is responsible for providing the Department with technical assessments and merit rankings of eligible applications.<sup>21</sup>

## Innovation Division and AusIndustry

**2.13** A Business Partnership Agreement between AusIndustry and Innovation Division of DITR articulates the two Divisions' responsibilities in the management and delivery of R&D Start. Appendix 1 describes the key responsibilities.

**2.14** Broadly, Innovation Division is responsible for providing policy advice to Government on R&D Start and evaluating the program's success in achieving its objectives. AusIndustry is responsible for the efficient delivery of the program, and supporting policy development and monitoring by providing relevant feedback, access to program data and recommendations on program design.

**2.15** The ANAO found that the Business Partnership Agreement clearly defines the roles and responsibilities of the two Divisions.

## Financial management framework

**2.16** R&D Start program expenditure is a component of the Department's annual appropriation for Outcome 2, *Enhanced economic and social benefits through a strengthened national system of science and innovation*. Within the appropriation, the Minister for Industry, Tourism and Resources sets an annual budget allocation for the program and formally notifies the Board of the amount.<sup>22</sup> Future year commitments of program funds are limited by a determination issued by the Minister for Finance and Administration.<sup>23</sup>

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<sup>20</sup> AusIndustry is responsible for the delivery of Commercial Ready.

<sup>21</sup> Commonwealth of Australia, *Commercial Ready Program Directions No 1 of 2004*, 30 August 2004, issued by the Minister for Industry, Tourism and Resources.

<sup>22</sup> This expenditure limit is also stipulated in the Industry, Tourism and Resources *Portfolio Budget Statements*.

<sup>23</sup> For example, under No. 2003/04, Determination under Financial Management and Accountability (*Amendments relating to Regulation 10*) Delegation 2003, issued in December 2003, 40 per cent of the Forward Estimates for the R&D Start program for 2005–06 can be committed prior to 2005–06.

## Financial and budget management arrangements prior to 2002

**2.17** Prior to 2002, the Board, or its committees,<sup>24</sup> approved a grant application, based on an assessment of its level of competitiveness. The approval decision formally committed R&D Start funds that had been allocated for the current and future years.

**2.18** Each year, following the setting of the annual budget allocation by the Minister, the Board set an annual grant approval target in two stages:

- Firstly, an estimate was made for the year of the amount required to meet existing grant payment commitments. This estimate was based on historical annual rates of spending for projects (spend rates), and the historical pattern of project expenditures likely to be deferred (or 'slipped') into later years (slippage rate).
- Secondly, the difference between the annual budget allocation and funds already committed provided an estimate of the level of new grant payments that could be approved. This amount was used to estimate the program's annual grant approval target.

**2.19** As the program had consistently underspent its annual budget allocation,<sup>25</sup> the Board adopted a strategy of inflating the estimated grant approval target, thereby over committing the program's annual budget allocation.<sup>26</sup>

**2.20** This approach aimed to minimise the size of the expected program underspend. However, it assumed that grant recipients would underspend their estimated annual project budgets, in line with historical patterns. In addition, few restrictions were placed on grant recipients regarding the way they managed their R&D project budgets. Consequently, spend and slippage rates were not easily controlled. This undermined AusIndustry's ability to accurately estimate commitments for the year, which, in turn, undermined the quality of the estimate for the annual grant approval target.

**2.21** In 2000–01, a record number and value of grants was approved: 233 grants valued at \$215 million, compared to an average of approximately \$165 million in approvals over the previous two years.

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<sup>24</sup> From May 2001 to November 2002, State and Territory Managers were authorised to approve small grants. Before then, the Executive General Manager or Head of Division was authorised to approve small grants.

<sup>25</sup> For example, in 1997–98, the program was \$63.24 million underspent.

<sup>26</sup> For example, the Board set \$180 million as the grant approval target for 2001–02. This level over committed the annual budget allocation by \$12 million.

## Over commitment of program funds in 2001–02

2.22 In 2001, grant recipients, overall, increased the rate at which they were spending the projects' approved budget. This change was not detected early enough by AusIndustry to advise the Board of the need to revise its grant approval strategy. AusIndustry did not regularly monitor grant recipient expenditure patterns through the year to confirm that the assumptions about project spend rates remained valid.

2.23 The combination of the large number of grants approved in 2000–01, and the increase in the rate of project expenditure by grant recipients in 2001 resulted in the program's annual budget allocation for 2001–02 being over committed by approximately \$60 million. See Figure 2.1.

**Figure 2.1**

### Annual budget allocation and actual expenditure, R&D Start grants, 2001–02 to 2004–05 (\$million)

| Level of expenditure     | 2001–02 | 2002–03 | 2003–04 | 2004–05 |
|--------------------------|---------|---------|---------|---------|
| Annual budget allocation | 144.7   | 142.0   | 168.2   | 174.9   |
| Actual expenditure       | 205.3   | 114.6   | 131.3   | 127.2   |

Sources: Industry Research and Development Board Annual Reports and AusIndustry

2.24 When it became evident in January 2002 that the program had insufficient funds in its annual budget allocation to meet grant payment obligations for the remainder of the year, the Board and its committees ceased approving new applications. The program was formally suspended to new applicants in May 2002 in accordance with ministerial directions.<sup>27</sup> It was reopened in November 2002.

2.25 To meet existing grant payment obligations, the Government approved an advance of \$40 million from future budget allocations for the R&D Start program. The balance of the funds shortfall was met by the reallocation of funds from other innovation programs within the Outcome 2 appropriation.

## Remedial actions

2.26 The Board and DITR agreed several reforms to the program's financial and budget management framework. These were implemented prior to R&D Start's reopening in November 2002. The reforms were designed to increase the Department's control of the commitment and expenditure of the program's annual budget allocation, within the existing legislative framework.

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<sup>27</sup> Commonwealth of Australia, *R&D Start Program Directions No 2 of 2002*, 7 May 2002.

**2.27** The most significant reform was the delegation by the Board of its authority to approve a grant to a senior executive officer in AusIndustry, called the Financial Delegate. The delegation centralised control of the management of the program's allocated funds in AusIndustry. As a result, the Department can control the commitment of R&D Start funds, and confirm that the program's expenditures will not exceed its annual budget allocation.

**2.28** Another key reform was the prohibition of a grant approval target exceeding the program's annual budget allocation. Under this reform, the decision to approve an application, and therefore commit program funds, is determined by the availability of uncommitted program funds at the time the decision is taken.

**2.29** In addition to reforms to AusIndustry's financial management arrangements, grant recipients are now given less flexibility in how they manage projects. Prior to 2002, grant recipients were permitted to accelerate or decelerate the progress of projects without discussing, with AusIndustry, the likely impact the variations could have on the rate at which they drew down their financial assistance. These arrangements undermined AusIndustry's ability to prepare, and then execute, an annual expenditure budget for the program.

**2.30** Since 2002, grant recipients have been required to define annual expenditure budgets for each year of the project. These budgets are specified in the grant Agreement and cannot be varied without approval. Also, grant recipients are required to provide AusIndustry with a quarterly expenditure profile for the project, which is updated every quarter as part of the progress reporting process. These arrangements provide AusIndustry with timely actual and estimated project expenditure information that enables it to manage the program's current and future year funds allocations.

**2.31** Overall, the ANAO found that the reforms implemented in 2002 by the Board and DITR provide a stronger assurance framework than the previous system for the program's expenditure to be managed within its annual budget allocation.

## **Performance management framework**

**2.32** The specification of an appropriate framework for measuring and monitoring performance is essential to enable assessment and management of progress towards the achievement of the program's objectives. Recognised better practice for performance information is to use an outcomes and outputs

framework, and to develop suitable performance indicators and targets that enable performance to be assessed.<sup>28</sup>

**2.33** DITR's framework<sup>29</sup> requires that performance measures are accurate, relevant, timely, and forward looking. In addition, performance measures should, wherever possible:

- highlight significant performance issues and risks, to allow timely action to be taken;
- relate to the program's objectives and outcomes; and
- include target levels of performance.

### **Program objectives**

**2.34** R&D Start's objectives define the outcomes the program is expected to have regarding the nature and extent of R&D activities in Australia. The program's objectives are to:

- (a) increase the number of projects involving R&D activities with a high commercial potential that are undertaken by companies;
- (b) foster greater commercialisation of outcomes of those projects;
- (c) foster collaborative R&D activities in industry, and between industry and research institutions;
- (d) encourage successful innovation in small companies by supporting commercialisation of internationally competitive products, processes and services;
- (e) increase the level of R&D activity in Australia that is commercialised in a manner that will benefit the Australian economy; and
- (f) increase the level of R&D activity conducted that provides national benefit.

### **Performance information**

**2.35** Innovation Division defines Key Performance Indicators (KPIs) for the program. They are specified in the Innovation Division–AusIndustry Business Partnership Agreement, where responsibility for collecting and reporting the KPIs is also addressed. The relationship between the program's objectives and the KPIs is not articulated in the Business Partnership Agreement. In response

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<sup>28</sup> ANAO *Better Practice Guide—Performance Information in Portfolio Budget Statements*, May 2002.

<sup>29</sup> This framework is articulated in the Business Partnership Agreement between the Innovation Division and AusIndustry, and is used for all programs under the *Backing Australia's Ability* initiative.

to this audit, DITR advised the relationship between the program's objectives and the KPIs is as described in Figure 2.2.

**Figure 2.2**

**Relationship between R&D Start's objectives and Key Performance Indicators**

| Key Performance Indicator  | Program objectives      |
|--|-------------------------|
| Number of projects progressed to commercialisation (i.e. from product to market)   | (b), (d)                |
| Amount of sales of new products, processes, services   | (e), (f)                |
| Change in the number of employees undertaking R&D  | (b), (d), (e), (f)      |
| Number of collaborative arrangements entered into through the project (including licences, joint ventures, partnerships, confidential disclosure agreements, domestic and foreign alliances) | (c)                     |
| Value of product, process or service developed under the program in one firm sold to other Australian firms  | (c)                     |
| Additional R&D expenditure resulting from the program that otherwise would not have occurred   | (a), (b), (d)           |
| Intellectual Property generated  | (e), (f)                |
| Number of people/organisations making initial inquiries to the program   | (a)                     |
| Additional funds/investment attracted from other sources   | (a), (b), (d), (e), (f) |

Source: AusIndustry

**2.36** The ANAO found that R&D Start's performance measurement framework has some limitations that affect its usefulness in measuring the achievement of the program's objectives.

**2.37** Relevant and meaningful KPIs enable the achievement of the program's objectives and outcomes to be measured. The relevance of some KPIs, including their ability to measure the achievement of outcomes, is not clear. For example, the four KPIs used to measure the achievement of the objective, 'encourage successful innovation in small companies by supporting commercialisation of internationally competitive products, processes and services' do not clearly indicate how the program's impact on **small** companies is measured, or the extent to which the products, processes or services that are commercialised by small companies are **internationally competitive**.

**2.38** In accordance with DITR's performance measurement framework for R&D Start, specific performance targets should be defined for the KPIs. Targets

were not set for R&D Start's KPIs. Such targets would provide a basis for accountability and performance improvement.<sup>30</sup>

**2.39** Improving the relevance of the KPIs for measuring achievement of program objectives and outcomes, and the setting of performance targets, will enhance DITR's capacity to measure and report on the achievement of the program's objectives.

## **Recommendation No.1**

**2.40** The ANAO recommends that AusIndustry and the Innovation Division of DITR strengthen the performance management framework for R&D Start and Commercial Ready by:

- improving the relevance of KPIs for measuring the achievement of program objectives and outcomes; and
- setting targets for KPIs, so that performance can be assessed.

### **DITR response**

**2.41** We accept the recommendation. Existing KPIs were established as part of the decision making to proceed with the Backing Australia's Ability initiatives. The rationale was that generic indicators would allow comparison of programs across different portfolios. DITR recognises the limitations of high level generic indicators and will consider how these could be supplemented with more specific KPIs and targets.

### **IR&D Board response**

**2.42** The IR&D Board is conscious of the need to enhance the link between KPIs and the program outcomes, and will continue to work with DITR on the issues raised by the ANAO.

### **Sources of performance data**

**2.43** Prior to 2004, two independent evaluations were used to measure the program's performance in achieving its objectives. The first evaluation was conducted in 2000, and the second was conducted in 2003.

**2.44** In 2004, AusIndustry commenced biannual surveys to collect information for a sub-set of the program's outcome measures and KPIs. In accordance with their grant obligations, R&D Start grant recipients whose grants finished one, two or five years previously were required to report on

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<sup>30</sup> For a discussion on performance targets, see ANAO *Better Practice Guide, Performance Information in Portfolio Budget Statements*, May 2002, Chapter 3.



commercialisation outcomes, and to provide information on the impact arising from participation in the program.<sup>31</sup>

**2.45** The response rates for the first two biannual surveys were low—for the first collection, 20 per cent of recipients whose reports fell due in the survey period responded; for the second collection, the rate was 26 per cent.<sup>32</sup>

**2.46** The ANAO found that AusIndustry does not have a target response rate for the biannual surveys, and has not undertaken a review to identify the reasons for the low response.

**2.47** Also, AusIndustry has not implemented strategies to encourage grant recipients to provide information that will enable the achievement of the program to be assessed, in accordance with their grant obligations.

**2.48** If grant recipients do not complete the biannual survey, there is a possibility of a non-response bias occurring if there is a significant difference in the characteristics of those who complete the survey, and those who do not.

**2.49** The ANAO acknowledges that non-response bias is a characteristic of all surveys. However, because grant recipients come from such a large cross section of business and industry, it is important to understand the impact of non-response on survey results.

**2.50** The non-response rates for the biannual surveys need to be regularly analysed to gauge the on-going reliability of the performance information. The inclusion of this analysis in any reports on the survey data would allow all users of the data to understand the nature of the non-response, and any associated bias.

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<sup>31</sup> Grant recipients sign an Agreement with the Commonwealth (see paragraph 5.1). It is a condition of the Agreement that the grant recipient must provide information and complete survey forms relating to the project when requested by the Commonwealth, for up to five years after the project is completed.

<sup>32</sup> AusIndustry advised that a further 14 per cent of reports were received after the due date.

## Recommendation No.2

2.51 The ANAO recommends that AusIndustry improve information available to evaluate program outcomes by:

- regularly analysing the non-response rate for biannual surveys of grant recipients to identify the nature of the non-response, and any associated bias;
- including this information in any reports of the survey data; and
- implementing strategies to encourage grant recipients to supply information requested by AusIndustry, in accordance with their grant obligations.

### DITR response

2.52 Agreed. DITR acknowledges that increased response rates would improve evaluation of program outcomes. DITR has commenced additional follow-up contact with non-responding grantees and commenced action to address the time lag associated with reporting on responses and the time of receiving responses. Whilst the response rate at the time of reporting on the biannual surveys is low, more reports are received after the reporting cut-off date. DITR notes that there were 234 respondents to these two surveys as reported, and considers that this response rate provides a reasonable basis to evaluate post project outcomes.

### IR&D Board response

2.53 The IR&D Board agrees with DITR's response.

## Results

2.54 Limitations in the performance data prevent judgments being made about the overall success of the program. Limitations include:

- the survey questions are not consistent across the evaluations (see paragraph 2.43) and biannual surveys. As a result, findings from the surveys cannot be consolidated to report a time-series of achievements against the program's objectives;
- the low response rates undermine the reliability of the performance information; and
- the lack of performance targets.

**2.55** Notwithstanding these limitations, survey results suggest that participation in R&D Start has produced positive results for respondents and the wider community. For example:

- the majority of respondents indicated that they would not have proceeded with the project without the R&D Start grant;
- 70 per cent of projects were successfully commercialised within one year of completing the R&D Start grant;
- additional sales resulting from participating in the program averaged \$1.2 million per respondent over the period 1999 to 2003;
- on average, respondents employed an additional three to four people to undertake the program-supported R&D activity; and
- the national economic benefits resulting from the program have been estimated at \$4.50 for every R&D Start dollar.<sup>33</sup>

**2.56** Conclusions about the extent to which the program has achieved its objectives cannot easily be made because of the lack of performance targets for the program's outcomes and Key Performance Indicators. These would assist in assessing how effectively the program is achieving its objectives.

## **Program outputs**

**2.57** Program quantity, quality and cost output measures are defined in the Innovation Division–AusIndustry Business Partnership Agreement, and include:

- quantity: number and value of applications received, considered and approved; and the number and value of payments processed;
- quality: level of customer satisfaction and performance against service standards defined in AusIndustry's Customer Service Charter; and
- cost: the administration cost of the customer entry process; application processing and decision process; and costs associated with ongoing grant recipient management.

**2.58** The ANAO found that most quantity and quality measures were reported monthly and quarterly by AusIndustry in accordance with the Business Partnership Agreement. The reports provided management with relevant information to monitor the program's delivery performance. Achievement of service performance targets for processing and deciding

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<sup>33</sup> Centre for International Economics, *Review of the R&D Start Program*, report prepared for the Department of Industry, Tourism and Resources, 17 September 2003, Chapter 4.

applications, making grant payments, and signing the grant Agreement are discussed in the relevant sections in this report.

**2.59** Detailed quantity output information is reported in the Board's annual reports, including: number and value of applications approved; approvals by industry sector; number and value of grants approved by company turnover; breakdown of approvals by grant size; and new grant agreements commenced in the year.

**2.60** However, the ANAO found that AusIndustry has not recently collected and reported cost output measures defined in the Business Partnership Agreement. AusIndustry advised that this resulted from the cessation, in 2001–02, of a departmental activity-based costing initiative due to its unreliability, compliance issues and cost. Detailed cost information on the three major components of the program's administration would assist AusIndustry to measure the program's efficiency, and identify possible cost savings.

**2.61** AusIndustry advised that systems are in place to collect and report on revised cost output measures for Commercial Ready. Two cost measures will be reported quarterly—the total cost of delivery of the program and the cost per grant. AusIndustry advised that these new cost measures will also be applied to R&D Start.

## **Conflict of interest and statement of private interest**

**2.62** The Board and committee members are drawn largely from the private sector. This provides commercial and technical expertise to inform decisions on an application's merits and its level of competitiveness. Inevitably, this means that many of these members have links to industry, creating a need to manage the risk of perceived or actual conflicts of interest (COI).

**2.63** For the Board and its committees, the Act requires disclosure of direct or indirect pecuniary interest by a member in a matter being considered, or about to be considered.<sup>34</sup> The Board's policies and procedures regarding the conflict of interest matters, and the recording of member private interests are documented in the *IR&D Board Handbook*, and published in its Annual Report.<sup>35</sup>

**2.64** AusIndustry administers the guidelines and maintains the register of members' private interest. The procedures preclude members receiving, or participating in consideration of, grant applications where there is a material conflict of interest.

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<sup>34</sup> *Industry Research and Development Act 1986*, Sections 16 and 24.

<sup>35</sup> Industry Research and Development Board, *Annual Report*, 2003–04, Appendix C.

**2.65** Over the period 2001–02 to 2004–05, one or more material<sup>36</sup> conflict of interest declarations were made by committee members in relation to approximately 30 per cent of decisions taken by committees. See Figure 2.3.

**Figure 2.3**

**Number of sectoral committee decisions with material conflicts of interest recorded, 2001–02 to 2004–05**

| Committee   | 2001–02     | 2002–03     | 2003–04     | 2004–05     |
|---|-------------|-------------|-------------|-------------|
| Engineering and Manufacturing<br>(% of decisions with COI)                    | 17<br>(20%) | 11<br>(15%) | 18<br>(17%) | 19<br>(20%) |
| Information Technology and<br>Telecommunications<br>(% of decisions with COI) | 26<br>(40%) | 6<br>(11%)  | 25<br>(23%) | 40<br>(35%) |
| Biological<br>(% of decisions with COI)                                       | 25<br>(46%) | 24<br>(53%) | 32<br>(55%) | 34<br>(57%) |

Source: AusIndustry

**2.66** The ANAO found that the Board’s Conflict of Interest and Statement of Private Interests policies are in accordance with recognised better practice principles,<sup>37</sup> and meet the requirements of Sections 16 and 24 of the Act. The ANAO observed the policies working well in practice—committee members did not receive applications for which they had declared a conflict of interest, and did not consider these applications during committee meetings.

**2.67** In addition, AusIndustry requires its officers who process R&D Start applications to complete an annual declaration that they will abide by its conflict of interest policies and procedures.<sup>38</sup>

## Management information system

**2.68** AusIndustry uses an electronic management information system to manage the delivery of R&D Start.<sup>39</sup> Overall, the system provides an effective management tool:

- the system’s functionality supports each of the key elements of the grant administration process, and is updated periodically to incorporate new or improved procedures;<sup>40</sup>

<sup>36</sup> *ibid.*, for a discussion on when a conflict of interest is material.

<sup>37</sup> See ANAO *Better Practice Guide—Public Governance*, 2004, Paper No. 6, *Conflicts of Personal Interest and Conflict of Role*.

<sup>38</sup> AusIndustry, *Conflict of Interest Guidelines*, November 2001.

<sup>39</sup> Funds commitments and grant payments are managed on the Department’s financial management information system, Finance One.

- comprehensive user documentation and expert advice on the system's operation are readily available to assist AusIndustry staff to enter and maintain the data base;
- the system captures most of the information required by AusIndustry to manage grant Agreements;
- data held on the system are reliable; and
- controls are built into the system that provide assurance AusIndustry staff administer R&D Start grants in accordance with the Board's policies, and procedures defined by AusIndustry.

## Summary

**2.69** Under the Act and ministerial directions, the Board is the approver of spending proposals. The Secretary of the Department is accountable, under the FMA Act, for the proper expenditure of public money appropriated to the Department.

**2.70** The Board has delegated most of the administrative activities for R&D Start to the three sectoral committees and AusIndustry. Documents outlining the delegations and the Board's policies and procedures provide a clear articulation of, and framework for, program administration.

**2.71** The Department did not have procedures in place to be assured that the Board, by approving spending proposals, had not over committed the program's allocation. This weakness resulted in the program over committing its allocation by \$60 million in 2001–02. The shortfall was met by a \$20 million reallocation of funds from other innovation programs, and an advance of \$40 million from future appropriations for R&D Start.

**2.72** Because of the over commitment of program funds, the Board ceased approving grants from January 2002. The program was formally suspended in May 2002. It was reopened in November 2002. Prior to its reopening, the Board and the Department put in place new financial management arrangements to prevent a reoccurrence of such over commitments. The key corrective action was the delegation of responsibility for the financial control of R&D Start funds to a senior executive officer of AusIndustry. However, the delegation did not resolve the overlap in the legislated financial management accountability for R&D Start between the Board and the Department.

**2.73** The legislative provisions relating to the Board's financial management responsibilities were removed from the Act and ministerial directions prior to

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<sup>40</sup> For example, AusIndustry added an additional payment control that requires the receipt of an annual audit certificate before a quarterly payment can be processed.

the commencement of the new Commercial Ready program in October 2004. Under the revised legislative arrangements, DITR is responsible for the administration of Commercial Ready.

**2.74** The program's performance measurement framework has some limitations that affect its usefulness in measuring the achievement of objectives and outcomes. For example, the relevance of some Key Performance Indicators to measure program outcomes is not clear. Also, specific targets have not been defined for Key Performance Indicators, to enable performance to be assessed.

**2.75** Prior to 2004, two independent evaluations were conducted to assess the program's effectiveness. In 2004, AusIndustry commenced biannual surveys to collect information on a sub-set of the program's outcome measures and Key Performance Indicators. A low response rate to the first two biannual surveys undermined the reliability of the initial results, as the results could not be readily extrapolated to the target grant population.

**2.76** Notwithstanding the limitations, the survey results suggest participation in R&D Start has produced positive results for grant recipients and the wider community.

**2.77** The Board and committee members are drawn largely from the private sector. This provides commercial and technical expertise to inform decisions. Inevitably, this means that many of these members have links to industry, creating a need to manage the risk of perceived or actual conflicts of interest.

**2.78** For the Board and its committees, the Act requires disclosure of direct or indirect pecuniary interest by a member in a matter being considered, or about to be considered. The ANAO found that the Board's Conflict of Interest and Statement of Private Interests policies are in accordance with recognised better practice principles, and meet the requirements of the Act. The ANAO observed the policies working well in practice.

## 3. Access to the Program

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*This chapter examines how effectively AusIndustry raised awareness of R&D Start through its promotion and marketing activities. It also examines how effectively AusIndustry assisted companies to access the program.*

### National Marketing Strategy

**3.1** Awareness raising for industry assistance programs,<sup>41</sup> such as R&D Start and its successor Commercial Ready, is guided by AusIndustry's National Marketing Strategy, adjusted for any specific requirements that arise during the year.

**3.2** The National Marketing Strategy provides the framework for AusIndustry to prepare and execute national, state and regional promotion and marketing plans. It outlines AusIndustry's awareness raising objectives (see Appendix 2) and promotion and marketing priorities.

**3.3** It also defines entities in the business community to be targeted by promotion and marketing activities, in order to maximise awareness levels of potential applicants. These entities include:

- decision makers in Australian companies that have demonstrated a willingness to innovate and enhance their international competitiveness;
- small business service providers;
- researchers; and
- accountants, lawyers, bankers, regional development organisations and industry associations that represent AusIndustry's target companies. These professional bodies and industry associations propagate information and advice about industry assistance to their many clients and association members.

**3.4** The ANAO found that, within the framework of the Strategy, AusIndustry has undertaken promotional activities to increase awareness of R&D Start. For example: AusIndustry delivered a comprehensive promotion strategy in the first half of 2002–03 for the reopening of R&D Start; in 2003–04, it promoted innovation programs, including R&D Start, by targeted advertising and media releases in industry-specific publications; and it

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<sup>41</sup> In July 2005, AusIndustry was delivering 35 industry assistance programs. (<<http://www.ausindustry.gov.au>> [accessed 26 July 2005])



presented 12 information seminars in 2004–05 to announce the closure of R&D Start and promote Commercial Ready.

3.5 A range of media are also used to disseminate program information to target audiences, including: advertising in industry and professional journals; public launches and special events; AusIndustry's website on the Internet; and direct electronic mail outs.

## Effectiveness

3.6 AusIndustry assesses the effectiveness of its awareness raising activities by conducting market and customer satisfaction surveys:

- market surveys collect information across all entities in the target audience; and
- customer satisfaction surveys<sup>42</sup> collect information from that subset of the target audience that has applied for financial assistance.

3.7 However, AusIndustry does not regularly measure and monitor the effectiveness of its awareness raising activities across all entities in the target audience. The most recent market survey<sup>43</sup> that measured awareness of R&D Start was conducted in 2002. It found that 71 per cent of businesses responding to the survey, and 67 per cent of professional bodies and industry groups were aware of the R&D Start program.

3.8 In the three Customer Satisfaction Surveys conducted since 2001, about 75 per cent of R&D Start applicants were satisfied with the promotion of the program, about 20 per cent were neither satisfied nor dissatisfied, and five per cent were dissatisfied.

3.9 As professional bodies and industry groups are a cost effective way to increase the awareness of potential applicants,<sup>44</sup> AusIndustry has targeted them in its awareness raising activities since 2002. For example, activities include the electronic mailing of innovation support program information directly to accounting firms and their representative bodies, sponsoring awards made by professional associations, and establishing and participating in networks with industry associations and in government economic development initiatives.

3.10 AusIndustry intended to conduct a follow-up market survey in 2004 to measure the impact its promotional activities had on its target audience. This

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<sup>42</sup> The most recent Customer Satisfaction Surveys were conducted in 2001, 2003 and 2004.

<sup>43</sup> The Wallis Group, *AusIndustry National Marketing Tracking Benchmark Study*, June 2002.

<sup>44</sup> A relatively small investment targeted at increasing awareness for professional bodies and industry groups has the potential to raise awareness in many of AusIndustry's potential applicants.

survey was not conducted because of resource constraints. AusIndustry advised that it is now scheduled for later in 2005.

**3.11** AusIndustry expended approximately \$8 million on awareness raising across its range of programs in the three years since the 2002 market survey. AusIndustry has measured, for a subset of the target audience,<sup>45</sup> the success of its recent initiatives to raise awareness. However, it has not measured their success across the rest of the target audience—for example, for professional bodies and industry associations.

**3.12** The ANAO considers that a strategy to regularly monitor the effectiveness of its awareness activities will enable AusIndustry to measure the success of its initiatives.

## Access

**3.13** Companies and research institutions that are aware of innovation support programs, and require more detailed assistance, can contact AusIndustry through three channels: AusIndustry's telephone Hotline; a Regional Manager; or a State or Territory office.

**3.14** For efficiency and quality control reasons, AusIndustry promotes the telephone Hotline as the primary point of contact for enquiries. Most enquiries (about 95 per cent) come through the Hotline. This frees skilled resources in the State and Territory offices to focus on the delivery of programs.<sup>46</sup> The use of scripted questions by Hotline operators facilitates quality and consistency of advice given to the caller.

**3.15** Performance of the Hotline and caller satisfaction with the service are monitored monthly. More than 90 per cent of callers surveyed between July and December 2004 rated the service as very good or better.<sup>47</sup>

**3.16** Hotline staff provide broad guidance of the enquirer's eligibility for an innovation program, and on the basis of this, refer potential applicants on for a more detailed assessment. The most suitable program is then identified and a Customer Service Manager (CSM) is allocated to the potential applicant. The first step in this process is for the CSM to contact the potential applicant to arrange a meeting.

**3.17** AusIndustry's aim in allocating a CSM is to create a single point of contact for the potential applicant, simplifying access to information and

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<sup>45</sup> That is, for companies that applied for financial assistance.

<sup>46</sup> As half of the approximately 21,000 calls to the Hotline in 2004 were unrelated to programs delivered by AusIndustry, State and Territory staff would be underutilised if they were the primary contacts.

<sup>47</sup> Surveys to measure Hotline caller satisfaction are conducted monthly.

advice. The ANAO found that AusIndustry placed a high priority on matching the CSM's skills with the potential applicant's project or, if possible, allocating a CSM to a potential applicant with whom they had worked previously.

**3.18** For example, in one state office, management reallocated a CSM from a different industry assistance program to assist a potential applicant because of the officer's experience with the proposed project's technology.

**3.19** Customer Satisfaction Surveys in 2003 and 2004 found approximately 80 per cent of respondents agreed that AusIndustry staff provided advice that was clear, consistent and comprehensive. Generally, applicants interviewed by the ANAO supported this finding. They advised that the allocated CSM was a valuable resource in deciding whether to proceed with an application and how best to present their case for funding support.

**3.20** AusIndustry set a performance target of two days for the CSM to contact the potential applicant to arrange an initial meeting. The ANAO found that State and Territory office managers regularly monitored the achievement of this performance target. In the NSW State Office, the average time for an allocated CSM to contact a potential applicant was three days. In approximately 60 per cent of cases, the time taken was two days or less.

**3.21** The ANAO also found that the achievement of the two day performance target was not reported to, or monitored by, R&D Start program management. AusIndustry have recognised this weakness and have implemented the necessary systems and procedures to enable Commercial Ready program management to monitor the achievement of the performance target.

## 4. Processing of Applications

*This chapter examines how a grant application was assessed, and the decision-making procedures for approving grants.*

### Introduction

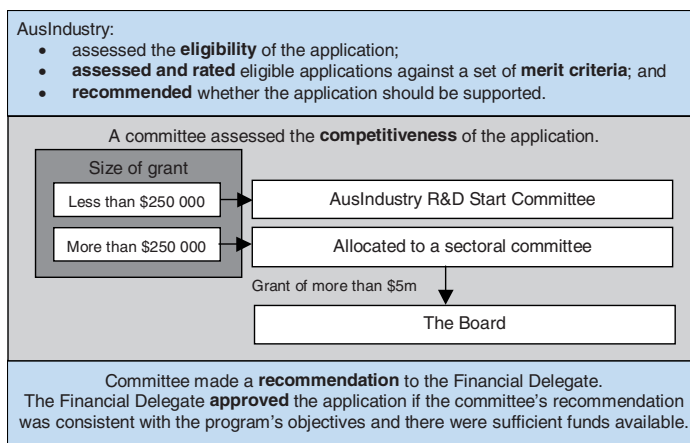
**4.1** The decision to approve or reject an R&D Start application was made in four stages. Firstly, AusIndustry confirmed that the application met the program's eligibility requirements.<sup>48</sup> Secondly, AusIndustry assessed the strengths and weaknesses of each eligible application, and provided the relevant committee with its assessment, as well as a recommendation on whether the application should be supported.

**4.2** In the third stage, having regard to AusIndustry's ratings, a committee assessed the project, and recommended to the Financial Delegate whether the project was sufficiently competitive to justify financial assistance.<sup>49</sup>

**4.3** The final stage of the process was the approval or rejection of the application by the Financial Delegate. Prior to approval, the Financial Delegate confirmed that the recommendation was consistent with the program's objectives and there were sufficient uncommitted funds to meet the new financial obligations. See Figure 4.1.

**Figure 4.1**

### Decision process for applications



Source: ANAO

<sup>48</sup> The Board delegated to AusIndustry the authority to reject ineligible applications.

<sup>49</sup> For grants of more than \$5 million, the committee's recommendation was further assessed by the Board before being sent to the Financial Delegate. Over the period 2001–02 to 2004–05, the Board considered 15 applications.

## Assessing eligibility

4.4 To be eligible for an R&D Start grant,<sup>50</sup> the applicant must:

- be a non-tax exempt company incorporated in Australia;
- be undertaking an R&D project that meets required levels of innovation and technical risk; and
- demonstrate it can fund its share of project costs.

4.5 To confirm the applicant's company status, AusIndustry advised that it searched the Australian Securities and Investment Commission's (ASIC) database. The ANAO found that AusIndustry did not consistently document the ASIC search findings on the project file. While the ANAO found no evidence that ineligible companies have received a grant, documentary evidence provides assurance for the committees and the Financial Delegate that the company is eligible for assistance.

4.6 The ANAO found that when the last two eligibility criteria could not be established clearly, AusIndustry forwarded the application to the relevant committee, drawing attention to its reservations about eligibility. Of the applications reviewed by the ANAO, approximately 60 per cent of those that were not supported by committees for eligibility reasons, were also not supported by AusIndustry.

4.7 To improve assessment of eligibility, especially in relation to establishing an applicant's ability to fund its share of project costs, AusIndustry implemented several initiatives. Financial skills development courses for CSMs were run in each State and Territory office in 2004–05. A Finance Working Group, consisting of senior State and Territory officers, monitored financial assessments undertaken by CSMs and recommended strategies to improve their quality. AusIndustry advised that a computer-based financial analysis tool is currently being developed to provide CSMs with a standard financial assessment methodology.

4.8 The efficiency of the assessment process would improve if CSMs were better able to reliably identify those applications that were ineligible, thereby reducing the number of applications forwarded to committees that are subsequently assessed to be ineligible. A review of eligibility assessments undertaken by CSMs on Commercial Ready applications would provide AusIndustry with a measure of the effectiveness of its initiatives to improve such assessments.

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<sup>50</sup> Eligibility for financial assistance under the R&D Start program is defined in Commonwealth of Australia, *R&D Start Program Directions, No.3 of 2002*, 28 November 2002.

## Assessing applications

**4.9** Ministerial directions defined the merit criteria (see Appendix 3) to be used to determine whether an application was sufficiently competitive to justify R&D Start funding support. Applicants were required to present their case for financial assistance by addressing each of the criteria.<sup>51</sup>

**4.10** A merit rating between 1 (low merit) and 6 (very high merit) was assigned to each criterion, and the individual merit ratings were then summed to give a total rating score that was used to determine competitiveness.

**4.11** The Board developed a detailed checklist of capabilities that would demonstrate an applicant was competitive against each merit criterion.<sup>52</sup> For example, to demonstrate the 'commercial potential of a project', the application would be assessed, *inter alia*, on whether it demonstrated clearly that there was:

- a strong, but realistic, market potential for the expected outcomes;
- a solid track record in commercialisation of R&D;
- a well articulated and suitable commercialisation strategy; and
- a thorough understanding of the competitive situation the new product will face.

## Assessment by AusIndustry

**4.12** The purpose of AusIndustry's assessment of an application's level of competitiveness was to provide committee members with relevant information and analysis to assist them to make an informed decision.

**4.13** The ANAO analysed the recommendations made by AusIndustry and the committees. In 2003–04, approximately 80 per cent of AusIndustry recommendations were the same as committee recommendations sent to the Financial Delegate. For 20 per cent (41 applications), committees recommended the application be rejected when AusIndustry recommended it be supported. There was only one instance where a committee recommended support, but AusIndustry did not.

**4.14** The ANAO found AusIndustry had no structured approach to analysing the reasons for the different recommendations so as to identify improvements that could be made to the quality of advice to committees.

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<sup>51</sup> Information on the merit criteria is publicly available on AusIndustry's website. The program's Customer Information Booklet and the Application Form provide detailed guidance on the criteria, and how committees will assess them.

<sup>52</sup> These capabilities are also listed in the R&D Start application form.

Quality advice provides assurance to a committee that the information provided in the application has been adequately analysed and any additional information that would assist the committee to assess the level of competitiveness has been provided.

**4.15** AusIndustry advised that, while it did not formally analyse its assessment process, program management monitored the consistency of the recommendations. When large or regular differences occurred, the reasons for the differences were reviewed. One outcome may have been additional training and guidance for the CSM. In addition, feedback on issues raised by committees was provided to senior State and Territory office staff after each round of committee meetings.

**4.16** The ANAO found that there was a pattern to the different recommendations. In 22 per cent of cases (nine applications) AusIndustry had recommended supporting the application where the total rating score was high, but it had given one merit criterion a rating of 2. Committees had not supported any of these applications. The committee decisions were consistent with procedural guidance<sup>53</sup> that states that applications may be declined where one criterion considered critical to the success of the project has a low level of merit.

**4.17** The ANAO considers that a more structured approach to analysing differences between AusIndustry and committee recommendations for the new Commercial Ready program would identify, in a timely manner, any patterns that may emerge. Additional training and guidance material could be identified that would improve AusIndustry's analysis and advice provided to committees.

## Recommendation No.3

**4.18** The ANAO recommends that AusIndustry undertake regular structured analysis of the reasons for any differences between AusIndustry and committee recommendations for the new Commercial Ready program, in order to develop strategies to improve the quality of advice given to committees.

### DITR response

**4.19** Agreed. DITR will continue to carry out the depth of analysis undertaken in relation to 2003–04 on an annual basis. As noted in the ANAO report, in 2003–04, approximately 80 per cent of AusIndustry

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<sup>53</sup> AusIndustry, *R&D Start Program Procedures Manual*, Version 6, 7 January 2005, Section 4.3.1, p. 28. Although this guidance is provided for consideration of small grants, sectoral committee Chairs advised that they apply the same decision process.

recommendations were the same as committee recommendations (para 4.13). DITR believes this is a significant and healthy correlation recognising that the committees have the technical and industry expertise whereas AusIndustry role is to provide well informed recommendations.

## **IR&D Board response**

**4.20** The IR&D Board agrees with DITR's response.

## **Assessment by committees**

**4.21** Committee members received, prior to a scheduled committee meeting, the application and AusIndustry's commentary and recommendation.<sup>54</sup> Having regard to AusIndustry ratings, each member reviewed the application, and assigned a merit rating for each criterion. At the meeting, a consensus was reached about the application's level of competitiveness and whether it was sufficiently competitive to justify financial assistance. Appendix 4 has a detailed description of the committees' appraisal procedures.

### *Appraisal procedures*

**4.22** It is important for the appraisal process to be transparent and free from the risk of claims of bias. Consequently, better practice requires all like applications to be assessed using a common process.<sup>55</sup>

**4.23** The Board documented appraisal procedures for the AusIndustry R&D Start Committee,<sup>56</sup> but not for the three sectoral committees. However, the ANAO found that each sectoral committee had developed substantially the same procedures for assessing an application's level of competitiveness.

**4.24** The lack of documented procedures for the sectoral committees has been addressed for Commercial Ready. An assessment framework document has been issued, and it provides guidance on the roles and responsibilities of the Board and the committees in assessing Commercial Ready applications, and the assessment methodology to be used.

### *Level of competitiveness justifying support*

**4.25** A common minimum total rating score across committees, or an articulated rationale for differing minimum ratings, provides assurance that committees have appropriately supported applications.

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<sup>54</sup> If a conflict of interest for an application has been declared, it is not distributed to the member.

<sup>55</sup> ANAO *Better Practice Guide—Administration of Grants*, May 2002, Canberra, pp. 42-47.

<sup>56</sup> Industry Research and Development Board, Policy A4, *R&D Start—Operating procedures for the AusIndustry R&D Start (RDS) Committee*, October 2003.



**4.26** The ANAO analysed all recommendations made by the four committees in 2003–04, and found that different scores were used when supporting applications:

- the Biological, and Engineering and Manufacturing Committees recommended support for applications that had a total rating score of 18 or more; and
- the Information Technology and Telecommunications, and AusIndustry R&D Start Committees recommended support for applications that had a score of 17 or more.

**4.27** Therefore, applications from the Engineering and Manufacturing, and Biological sectors were required to have a higher level of competitiveness than applications from the Information Technology and Telecommunications sector, and for applications less than \$250 000.

**4.28** The ANAO found that the different levels of competitiveness were not based on a risk, merit-based or other rationale, nor was the reason for the different levels documented. Although the observed difference in the rating was small, the lack of a rationale for the difference undermines transparency and risks claims of bias. There is also a risk that the difference could increase over time, resulting in applications from different industry sectors being subjected to quite different standards of competitiveness without a clear reason why.

**4.29** A common minimum total rating score has not been established for Commercial Ready applications. A clearer and documented rationale for the minimum total rating score required to support an application would enhance transparency for, and accountability to, stakeholders in Commercial Ready.

## **Recommendation No.4**

**4.30** The ANAO recommends that, for transparency and accountability to stakeholders, committees apply consistent minimum total rating scores to Commercial Ready applications, or a rationale for any differences be documented.

## **DITR response**

**4.31** Agreed. The IR&D Board and DITR have adopted a consistent minimum total rating score. At the same time, DITR notes that in any assessment process involving a range of views, there will always be some degree of disparity in overall scores reflecting individual judgments.

## **IR&D Board response**

**4.32** The IR&D Board agrees with DITR's response.

### *Conditioning approvals*

**4.33** In reaching agreement to support an application, the committee may have qualified the approval by placing conditions on the applicant. These conditions mitigated the risk associated with the project. The applicant had to satisfy the conditions before the grant contract was finalised.<sup>57</sup>

**4.34** Two thirds of conditions placed on supported applications in 2004–05 related to financial issues, such as requiring documentary evidence that a loan facility was in place, or that the company could match funding for the project.

**4.35** The ANAO found that procedural guidance was not provided to committees advising when it was appropriate to place a condition on an applicant to mitigate a risk, or when it was more appropriate to reject the application. Without guidance, there is a risk that committees may make inconsistent decisions.

**4.36** This weakness has been addressed for Commercial Ready. The program's assessment methodology requires committees to make recommendations that reflect the merit of the application, rather than placing conditions on recommendations to address risks in applications.<sup>58</sup>

### *Proportion of applications supported by committees*

**4.37** Variations between the proportions of applications supported by committees could be attributable to either the selection procedures used by individual committees, or to other factors, such as the quality of applications assessed.

**4.38** The ANAO found that the Board and AusIndustry do not undertake regular comparative analyses of the proportions of applications supported by committees. The ANAO reviewed the proportions over the period 2001–02 to 2004–05. See Figure 4.2.

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<sup>57</sup> Over the four years 2001–02 to 2004–05, approximately 40 per cent of supported applications had conditions placed on them.

<sup>58</sup> AusIndustry, *Assessment Framework—Commercial Ready Program*, September 2004.

**Figure 4.2****Proportion of applications supported by committees (per cent), 2001–02 to 2004–05**

| Committee                                     | 2001–02   | 2002–03   | 2003–04   | 2004–05   |
|---|-----------|-----------|-----------|-----------|
| Engineering and Manufacturing                 | 49        | 63        | 68        | 50        |
| Information Technology and Telecommunications | 36        | 44        | 58        | 42        |
| Biological                                    | 36        | 68        | 66        | 56        |
| AusIndustry R&D Start                         | n/a       | 75        | 75        | 46        |
| <b>Total</b>                                  | <b>40</b> | <b>61</b> | <b>65</b> | <b>48</b> |

Source: AusIndustry

Notes: In 2001–02, decisions on grants for less than \$500,000 were delegated to State/Territory Office Managers. They approved 43 of 71 applications (61 per cent).

Statistics for 2001–02 exclude 88 applications that were deemed rejected when the program was temporarily suspended.

**4.39** Because of unusual circumstances, the proportions of applications supported by committees in 2001–02 and 2004–05 were lower than in the intervening years:

- in 2001–02, the over commitment of the program's funds, and subsequent temporary suspension of the program, resulted in a higher than normal number of applications being rejected; and
- in 2004–05, after the announcement of the closure of the program, many companies submitted applications that had been prepared quickly to meet the closing date. Consequently, applications were, on average, of lower quality, resulting in a higher than normal proportion of applications being recommended for rejection.

**4.40** The proportion of applications supported by the Information Technology and Telecommunications Committee was lower than other committees. AusIndustry advised that this is likely to be a result of this committee receiving a higher rate of less meritorious applications than other committees. The Committee Chair advised that determining eligibility and assessing the technical strength merit criterion of software-related R&D projects is challenging. To assist in this regard, the Committee provided additional guidance for potential applicants on the types of software developments likely to be considered R&D.<sup>59</sup>

<sup>59</sup> AusIndustry, *R&D Start Program, Guidelines of R&D in Relation to Computer Software Development*, September 2003.

**4.41** On the other hand, small grant applications had a relatively high rate of support (by the AusIndustry R&D Start Committee). Available data on project outcomes indicate that these smaller grant projects also had a higher rate of subsequent commercial success. Data indicate that 77 per cent of projects receiving grants of \$200 000 or less had been successfully commercialised five years after completion of the grant, compared to 31 per cent for projects receiving grants greater than \$200 000.<sup>60</sup>

**4.42** The ANAO considers that regular comparative analyses of the proportions of applications supported by committees, linking approval rates to the subsequent success rates of projects, would provide greater assurance that appraisal procedures are conducted in a consistent manner. With the commencement of biannual surveys of grant recipients, the information required to conduct such analyses will be readily available.

## **Recommendation No.5**

**4.43** The ANAO recommends that AusIndustry strengthen quality assurance by:

- evaluating committee recommendations for Commercial Ready grant applications to identify reasons for differing rates of approval across committees; and
- assessing the extent to which any differences are reflected in the subsequent commercial success of projects.

### **DITR response**

**4.44** Agreed. DITR will continue to monitor committee meetings to ensure consistency of approach with scoring and assessment methodology. DITR notes, however, there could be a number of legitimate reasons for differences in approaches by committees including the characteristics of the particular industry sectors and the quality of applications generally. Nevertheless, DITR currently assesses technical and commercial success of projects and is able to make the comparison recommended between committees.

### **IR&D Board response**

**4.45** The IR&D Board agrees with DITR's response.

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<sup>60</sup> Results are from AusIndustry's biannual surveys. These were discussed in Chapter 2.

## Approval by the Financial Delegate

**4.46** As discussed previously, since 2002, the Financial Delegate was required to confirm a committee's recommendation was consistent with the program's objectives, and sufficient program funds were available to meet the financial obligations resulting from the approval of a grant application.

**4.47** The ANAO found that, for the applications examined, the Financial Delegate approved grants in accordance with the financial management delegation.

**4.48** In addition, procedures were introduced in 2002 that outlined the process for selecting grants if insufficient funds were available to fund all the applications supported by a round of committee meetings. In these circumstances, the Committee Chairs were required to prioritise the applications from all committees, and the Financial Delegate was to select the highest priority applications that could be funded from the program's remaining uncommitted funds.

**4.49** AusIndustry and the Committee Chairs advised that, since the introduction of the new financial management arrangements in November 2002, sufficient uncommitted funds had been available to approve all committee-supported applications.

### Timeliness of application processing and approval

**4.50** AusIndustry and the Board set a performance target of 60 days for processing, assessing and deciding a grant application.

**4.51** The proportion of applications processed and decided within the 60-day target improved over the period 2001–02 to 2003–04 from 57 per cent to almost 70 per cent. See Figure 4.3. The decline in performance in 2004–05 was a result of an influx of applications after the announcement of the closure of the program.

**Figure 4.3**

#### Performance in processing and deciding on an application, 2001–02 to 2004–05 (per cent)

| Performance measure-proportion of applications processed and decided within: | 2001–02 | 2002–03 | 2003–04 | 2004–05 |
|--|---------|---------|---------|---------|
| 60 days  | 57      | 69      | 68      | 39      |
| 75 days  | 71      | 87      | 82      | 43      |

Source: AusIndustry

**4.52** The 60-day target was not increased after the addition of the Financial Delegate approval procedure in 2002. This additional step added, on average, 12 days to the application processing and approval process.

**4.53** To take account of this additional step, AusIndustry increased the processing and approval performance target to 75 days for Commercial Ready applications. Decisions in over 80 per cent of R&D Start applications in 2003–04 were made within 75 days, indicating that it is a more realistic target, but one where improvements could still be achieved.

**4.54** Applicant satisfaction with AusIndustry's adherence to agreed timeframes has been high. In the 2004 Customer Satisfaction Survey, over 90 per cent of those surveyed were satisfied with the performance of AusIndustry staff in meeting agreed timeframes.<sup>61</sup> Also, applicants interviewed by the ANAO were satisfied with AusIndustry's performance in this regard. In particular, they highlighted the way AusIndustry notified them of changes to agreed timelines, and the reasons for the changes.

## Notification of decision

**4.55** Following the Financial Delegate's decision, AusIndustry promptly notified applicants, by telephone, and confirmed the decision with a formal decision letter. The ANAO found that, in 2004–05, the average time taken to send the decision letter was five days.

**4.56** In recent years, the formal notification for unsuccessful applicants provided limited information on the reasons for the rejection.<sup>62</sup> Only 14 per cent of unsuccessful applicants surveyed in the 2004 Customer Satisfaction Survey were satisfied with the written advice they were given about the rejection.

**4.57** However, 30 per cent of unsuccessful respondents were satisfied with the adequacy of the feedback given by CSMs when contacted to discuss the reasons for the rejection.

**4.58** The Board and AusIndustry noted the high levels of dissatisfaction with the written and oral explanations given to unsuccessful applicants. Decision letters for Commercial Ready include more specific details on the committee's reasons for assessing an application as uncompetitive.

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<sup>61</sup> R&D Start, *Customer Satisfaction Survey Report*, April 2004, p. 22.

<sup>62</sup> In most cases, the merit criteria that contributed to the application being assessed as uncompetitive were listed.

## 5. Contractual Arrangements for Grants

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*This chapter examines whether the R&D Start Deed of Agreement provides a sound accountability framework for the management of grants.*

### Introduction

**5.1** The Board, on behalf of the Commonwealth, established a formal contractual arrangement with the successful applicant(s) before grant payments commenced.<sup>63</sup> This contract is called a Deed of Agreement (the Agreement).

**5.2** In finalising the terms and conditions of an Agreement, the applicant was required to satisfy any special conditions placed on the grant approval by the Financial Delegate as recommended by the committee. Also, any changes requested by the applicant to an approved project's technical and financial plans were to be reviewed by AusIndustry and approved by the relevant authority.

### The Agreement

**5.3** AusIndustry used a template document to produce the Deed of Agreement. It consisted of two parts:

- a General Conditions document that defines a standard set of rights and obligations for each party to the Agreement, such as the obligations of the grant recipient in respect of the transfer of Intellectual Property, and the rights of the Commonwealth to terminate the Agreement; and
- a Particular Conditions document that outlines project specific terms and conditions on which the grant is made. For example, it defines: the project's planned outcomes; the start and finish dates for the project; the total amount of the grant and the annual grant payment limits; the agreed project costs and milestones; and a schedule of progress and other reports to be submitted by the grant recipient.

**5.4** The ANAO found that the Agreement provides sufficient information to allow AusIndustry to determine that the grant is used for the agreed purpose, and that grant payments are made according to progress of the

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<sup>63</sup> The ministerial directions stipulate this requirement. See Commonwealth of Australia, *R&D Start Program Directions No 3 of 2002*, dated 28 November 2002, s.18. The Board delegates its authority to sign Agreements to senior officers in AusIndustry.

project.<sup>64</sup> It also clearly articulates the requirements that must be met by the grant recipient for grant payments to be made.

## Producing the Agreement

5.5 AusIndustry procedures required a CSM to confirm, prior to producing the Agreement, that the applicant had satisfied any special conditions placed on the grant approval. For the Agreements it examined, the ANAO found that additional information required by the special conditions had been provided by the applicant and approved by the appropriate delegate.

5.6 Also, the ANAO found that most terms and conditions, such as project start and finish dates, timings of milestones and annual expenditure profile, were accurately reflected in the Agreements examined.

5.7 However, in some of these Agreements, due dates for progress reports were inconsistent with the program's reporting guidelines. For example, some due dates for end-of-project reports were set to 28 days after the project's completion date, while 42 days was stipulated in the guidelines.<sup>65</sup> While the impact of this inconsistency is minor on the management of the grant, clear terms and conditions minimise the risk of grant recipients misunderstanding their obligations under the Agreement.

5.8 The alignment of dates listed in the Agreement with the reporting guidelines would enhance clarity.

## Signing the Agreement

5.9 The ANAO found that, for the Agreements it examined, they were signed in accordance with the Board's requirements.<sup>66</sup> The ANAO noted that, in a small number of cases, pages of documents had not been initialled,<sup>67</sup> in accordance with procedures. Failure to initial pages of key documents does not invalidate the Agreement. However, the procedure provides assurance that all parties had received key documents and understood the obligations defined in them. Monitoring adherence to the procedure is warranted.

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<sup>64</sup> ANAO *Better Practice Guide—Administration of Grants*, May 2002, Chapter 4.

<sup>65</sup> AusIndustry, *R&D Start Program, Grants for R&D Projects, Project Reporting Guide*, September 2004.

<sup>66</sup> Two company directors, or one director and the company secretary, must sign the Agreement to give full protection to the Commonwealth that the Agreement can be relied upon as the will of the company.

<sup>67</sup> All parties to the Agreement are required to initial all pages of the Particular Conditions of the Agreement, and the front page of the Project Reporting Guide and Eligible Expenditure Guidelines.



## Signing within the performance target

**5.10** The timely signing of an Agreement reduces the risk of program expenditures slipping into the next fiscal year.<sup>68</sup> This assists AusIndustry to manage the program's annual budget allocation.

**5.11** Prior to 2003–04, the target time for an Agreement to be signed was within 90 days from the date of formal notification.

**5.12** From 2003–04, the target time was within 30 days of formal notification. AusIndustry advised that the reduced target aimed to encourage successful applicants to expedite the signing of the Agreement. If the Agreement could not be signed within the 30-day target, the Financial Delegate was required to approve a new deadline.

**5.13** In 2002–03, 86 per cent of Agreements were executed within the 90-day target time. In 2004–05, 78 per cent of Agreements were signed within the 30-day target time, or the new time agreed by the Financial Delegate. See Figure 5.1. The ANAO found that, in the Agreements examined, requests for an extension of time were appropriately approved.

### Figure 5.1

#### Timeliness of signing R&D Start Agreements, 2002–03 to 2004–05

| Performance   | 2002–03 | 2003–04 | 2004–05 |
|---|---------|---------|---------|
| Proportion of Agreements signed within agreed target (per cent) | 86      | 75      | 78      |

Source: AusIndustry

**5.14** For the Agreements examined by the ANAO, delays in signing were, generally, the result of special conditions applied to approvals. The Commercial Ready assessment framework requires committees to assess applications on merit at the time of the application, as special conditions will not be set in Commercial Ready Agreements.<sup>69</sup> One expected outcome from this new policy is the reduction in time for an Agreement to be signed.

**5.15** The ANAO considers monitoring the achievement of the 30 day performance target for Commercial Ready would allow AusIndustry to confirm that the new assessment framework has been effective in reducing the time taken to sign grant Agreements.

<sup>68</sup> Grant payments cannot commence until all parties to the Agreement sign it.

<sup>69</sup> AusIndustry, *Assessment Framework—Commercial Ready Program*, September 2004.

## 6. Compliance with the Contractual Arrangements

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*This chapter examines how effectively AusIndustry and grant recipients meet their obligations under the Deed of Agreement, including the effectiveness of the reporting, payment and acquittal processes.*

### Introduction

**6.1** Following the signing of the Agreement, the grant recipient reports to AusIndustry each quarter on the project's progress. If progress is assessed as satisfactory, AusIndustry makes quarterly payments to the grant recipient.

**6.2** Variations to the Agreement during the life of the project, such as extensions of time, are processed by AusIndustry and approved by the appropriate delegate.

**6.3** At the end of the project, AusIndustry verifies the outcome of the project is in accordance with the Agreement, and if so, approves the final payment of the grant.

### Progress reports

#### Risk management

**6.4** AusIndustry manages the risk that a project may receive grant funding without satisfactory achievement of its milestones, by requiring each recipient to report on their project's progress each quarter, and at the end of the project. Grant payments are not made until a satisfactory progress report<sup>70</sup> is submitted. Progress reports include:<sup>71</sup>

- an update on the project's technical and commercial progress achieved, and that expected for the remainder of the project;
- an expenditure report, detailing eligible expenditure incurred over the reporting period; and
- for quarterly reports, an adjusted budget for the remainder of the project.

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<sup>70</sup> A progress report is considered satisfactory if it contains all the information that is required by AusIndustry: to confirm that technical progress is being achieved; and to calculate the amount of the next grant payment.

<sup>71</sup> Reporting guidance material provided to the grant recipient describes the format and detail required.

**6.5** Grant recipients are required to submit satisfactory progress reports by the due date specified in the Agreement.

**6.6** AusIndustry has a control in the grants management information system that precludes a quarterly grant payment being made until a satisfactory progress report has been received, and recorded in the system.

**6.7** AusIndustry also assigns a high, medium, or low risk rating to each project when the Agreement is signed. The rating is reviewed, and adjusted if necessary, on receipt of each quarterly progress report. The rating assists State and Territory office management to determine the amount of effort required to monitor a project in order to maximise the probability of an acceptable outcome.

**6.8** AusIndustry reviews the reported progress against the expected achievements outlined in the Agreement, and ensures that the level of eligible expenditures claimed for that quarter is in accordance with progress and the budget in the Agreement. When calculating each quarterly payment, the last quarter's actual expenditure is reconciled with the previous grant payment made,<sup>72</sup> and the current quarter's payment is adjusted for any resulting differences. Each payment aims to maintain the Commonwealth's level of contribution to the project's expenditures defined in the Agreement.

**6.9** Late reports delay quarterly payments, and ultimately can result in grant expenditures budgeted for the current year being forced into the following year. This increases the risk that the program's annual budget allocation will be underspent.

### **Providing progress reports by the due date**

**6.10** Since the reopening of R&D Start in November 2002, AusIndustry has increased its monitoring of grant recipients' compliance with their reporting obligations. For example, recipients have been reminded by telephone, email or formal correspondence of the due dates of their progress reports.

**6.11** The increased monitoring has led to improved compliance. The proportion of grant recipients submitting progress reports by the due date almost doubled from 31 per cent in 2001–02 to 60 per cent in 2004–05. See Figure 6.1. For end-of-project reports, the proportion increased to 58 per cent.

**6.12** Overdue reports have little impact on the program in the short term as AusIndustry does not make a grant payment without a report having been received and assessed. Where a grant recipient fails to submit an overdue progress report on request from AusIndustry, the Board may terminate the Agreement and seek recovery of grant payments not acquitted. AusIndustry

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<sup>72</sup> Grant payments are made in advance.

advised that, to date, no such sanctions have been imposed on a grant recipient for late reporting.

**Figure 6.1**

**Progress reports, 2001–02 to 2004–05**

| Progress reports                                     | 2001–02 | 2002–03 | 2003–04 | 2004–05 |
|--|---------|---------|---------|---------|
| No. of reports received:                             |         |         |         |         |
| quarterly reports                                    | 1,239   | 956     | 873     | 974     |
| end-of-project reports                               | 202     | 199     | 158     | 119     |
| Proportion of reports received by due date:          |         |         |         |         |
| quarterly reports                                    | 31%     | 33%     | 51%     | 60%     |
| end-of-project reports                               | 43%     | 46%     | 61%     | 58%     |
| Average time to achieve 'satisfactory' status (days) |         |         |         |         |
| quarterly reports                                    | 27      | 33      | 27      | 21      |
| end-of-project reports                               | 19      | 26      | 41      | 22      |

Source: AusIndustry

**6.13** As discussed in paragraph 6.9, late reports can result in the program’s annual budget allocation being underspent. An evaluation of the reasons for late reporting would assist AusIndustry to develop and implement strategies to improve the timeliness of reporting by grant recipients, and assist in the management of the budget.

**6.14** In 2004–05, for reports found to have insufficient information to enable AusIndustry to assess project progress, it took an additional 21 days on average for recipients to supply the extra information required. See Figure 6.1. Some recipients advised the ANAO that, for the first one or two progress reports, they had not initially understood the reporting requirements, and AusIndustry guidance did not provide sufficient practical examples for their project.

**6.15** The ANAO suggests that AusIndustry examine the provision of additional guidance to grant recipients to reinforce its requirements.

**Site visits**

**6.16** Assessment of progress reports can be done by either a desk audit of the claims made in the report or visiting the grant recipient.

**6.17** AusIndustry has a risk management strategy to manage the risks associated with managing R&D Start projects. This strategy defines the

circumstances when a site visit may be appropriate to assess a project's progress. These include:

- when the project is classified as high risk;
- if significant changes to a project have occurred that could undermine the grant recipient's ability to meet the terms and conditions of the Agreement;<sup>73</sup> and
- at the end of the project.

**6.18** Clear guidance on when site visits should be conducted to assess a project's progress, and achievement of targets for site visits, provides assurance that project risks are being managed in a manner consistent with the program's risk management strategy.

**6.19** The ANAO found that the targets for site visits are inconsistent across different components of the risk management strategy.

**6.20** Firstly, in AusIndustry's compliance management strategy,<sup>74</sup> a project's assessed risk determines the frequency of a site visit. All high-risk projects are to be visited at least annually, and medium and low risk projects are to be visited less frequently. The strategy states:

- for low-risk projects, a site visit is to be conducted within the first year, then possibly at the end of the project;
- for medium-risk projects, a site visit is to be conducted within the first year, and then at the end of the project; and
- for high-risk projects, a site visit is to be conducted at six months, then at least annually.

**6.21** Secondly, AusIndustry's 2004–05 annual compliance plan for site visits set a target of 100 per cent of **all** grant recipients to be visited once a year. That is, irrespective of their risk rating, all projects are to be visited.

**6.22** AusIndustry did not achieve the targets. For instance, approximately 60 per cent of **all** projects were visited in 2004–05, and only 25 per cent of high risk projects were visited.

**6.23** There is discretion to conduct end-of-project visits for low-risk projects. However, AusIndustry does not monitor the use of that discretion, despite this being the last opportunity for AusIndustry to assure itself that projects

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<sup>73</sup> For example: if the company experiences financial difficulties; if there is a change in key project personnel; late or unsatisfactory reporting; inconsistent reporting; or significant over or under spending to achieve milestones.

<sup>74</sup> AusIndustry, *Compliance Management Strategy—2004–05*.

achieved the outcomes in accordance with Agreements. Over the period 2001–02 to 2004–05, AusIndustry visited approximately half of the projects at their completion. See Figure 6.2.

**Figure 6.2**

**End-of-project visits conducted for Core Start and Start Plus grants, 2001–02 to 2004–05**

| End-of-project visits  | 2001–02 | 2002–03 | 2003–04 | 2004–05 |
|--|---------|---------|---------|---------|
| No. of end-of-project reports for Core Start and Start Plus grants | 188     | 184     | 151     | 70      |
| Proportion where end-of-project visit was undertaken               | 35%     | 53%     | 46%     | 61%     |

Source: AusIndustry

**6.24** The setting of clear and consistent targets will assist managers to identify the program’s risk management priorities, and to plan their compliance activities. Achievement of these targets, and monitoring the use of discretion, provides assurance that the identified project risks are being managed in accordance with AusIndustry’s risk management strategy.

**6.25** AusIndustry advised that the program’s 2005–06 compliance management strategy will include clearer guidance on conducting visits. Also, visit targets will be adjusted, taking into account performance in 2004–05, resourcing priorities, and feedback from State and Territory offices.

**Recommendation No.6**

**6.26** The ANAO recommends that AusIndustry set clear and consistent site visit targets for Commercial Ready and R&D Start projects, and where discretion for conducting visits is allowed, monitor the use of such discretion in order to inform decisions about the targets.

**DITR response**

**6.27** Agreed. DITR acknowledges that targets set in previous years may have been overly ambitious given the resources available to manage the program. Risk management based targets have been set for 2005–06 and we will monitor the exercise of discretion in conducting visits.

**IR&D Board response**

**6.28** The IR&D Board agrees with DITR’s response.

## Grant payments

6.29 After assessing technical progress and eligible expenditure claims, AusIndustry calculates the next grant payment.

### Payment calculation

6.30 The ANAO found that the steps in calculating the level of the payment are adequately defined in the Procedures Manual. Proformas and checklists are used to ensure all steps are undertaken, and worksheets were generally recorded on project files.

6.31 The grants management information system is used to calculate and control payments, increasing the assurance that payments have been calculated and approved accurately.

6.32 The payments examined by the ANAO were made according to the approved amounts set out in Agreements, or had been appropriately varied (see paragraphs 6.44 to 6.48). Also, payment calculations were generally appropriately checked and authorised, and retained on the project file, providing an audit trail.

### Confirmation of eligible expenditure

6.33 AusIndustry does not confirm that project expenditures claimed in quarterly progress reports comply with the program's eligible expenditure guidelines. Instead, it relies on an annual audit certificate issued by an independent auditor appointed by the grant recipient.<sup>75</sup>

6.34 The purpose of the independent audit is to provide reasonable assurance that the expenditures reported by the grant recipient were spent for the purposes of the project in accordance with the Agreement, and complied with the definition of eligible expenditure provided in the guidelines.

6.35 In projects examined by the ANAO, AusIndustry reduced the grant recipient's next quarterly payment if the independent auditor found ineligible expenditure had been claimed. For example, one grant recipient had claimed the total cost of a new computer, rather than the annual depreciation. AusIndustry correctly deducted the extra expenditure claimed from the next quarter's payment.

6.36 CSMs are required to check the audit certificate has been received by its due date, prior to making the next quarterly payment. The ANAO found instances when a quarterly grant payment had been made without an audit

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<sup>75</sup> Audit reporting requirements are specified in AusIndustry, *R&D Start Program, Grants for R&D Projects, Project Reporting Guide*, September 2004.

certificate having been received. To address this weakness, AusIndustry introduced, in June 2005, a control in the grants management information system to prevent a quarterly payment being made if an audit certificate is overdue.

**6.37** As part of its compliance management strategy, AusIndustry is planning to implement an audit program that aims to substantiate the veracity of independent audit certificates submitted by the grant recipients. To finalise its audit strategy, AusIndustry planned to conduct 20 audits as a pilot in 2004–05, but only conducted nine. At the time of the ANAO’s audit, AusIndustry had not completed an analysis of the findings of these audits, nor determined whether they had sufficient information to develop a strategy for the program.

**6.38** Because of AusIndustry’s reliance on the independent audit certificate to confirm the grant recipient’s compliance with the Agreement, the timely introduction of the planned program of substantiation audits would provide increased assurance that grant payments are being made in accordance with grant Agreements. In response to the draft audit report, AusIndustry advised that, following an analysis of the results of the nine completed audits, it has set a target of 12 substantiation audits for 2005–06.

### **Making payments on time**

**6.39** To provide assurance to grant recipients that progress reports and payments would be processed expeditiously, AusIndustry set a 30-day target to make grant payments. The ANAO found that AusIndustry’s performance has improved from 78 per cent of payments being made within the target in 2001–02, to 80 per cent in 2004–05. See Figure 6.3.

**Figure 6.3**

#### **Grant payments made within the 30-day performance target, 2001–02 to 2004–05**

| <b>Grant payments</b>          | <b>2001–02</b> | <b>2002–03</b> | <b>2003–04</b> | <b>2004–05</b> |
|--------------------------------|----------------|----------------|----------------|----------------|
| No. of payments processed      | 1,251          | 947            | 892            | 947            |
| Proportion paid within 30 days | 78%            | 76%            | 84%            | 80%            |

Source: AusIndustry

**6.40** The ANAO found that, in the projects it reviewed, the main reason for AusIndustry not meeting the target was to process variations, such as the reallocation of funds between years, arising from the reported progress.



**6.41** In the 2003 and 2004 Customer Satisfaction Surveys, 96 per cent of respondents were satisfied with AusIndustry's administration of their R&D Start grant, including the timeliness of grant payments.<sup>76</sup>

### Acquitting the final payment

**6.42** If the last quarterly payment prior to completion of the project is greater than the actual expenditure incurred for that quarter, then an overpayment could occur. To minimise the risk of an overpayment, AusIndustry withholds five per cent of the total grant until the end-of-project report is received, and a final project acquittal has been completed. If the five per cent is insufficient to cover the overpayment, then the remaining amount is sought from the grant recipient.

**6.43** The ANAO found that over the three years 2002–03 to 2004–05, \$2.5 million, out of \$373 million total grant payments, was overpaid to grant recipients. See Figure 6.4. AusIndustry advised that it has not increased the five per cent retention amount because grant recipients have, in general, repaid the overpaid grant in a timely manner. Approximately 83 per cent of the overpayments in 2004–05, and 43 per cent in 2003–04 have been repaid. Debt recovery practices are followed by DITR when the debt has reached 90 days.

**Figure 6.4**

#### Grant overpayments, 2001–02 to 2004–05

| Overpayments/repayments     | 2002–03 | 2003–04 | 2004–05 |
|-----------------------------|---------|---------|---------|
| Number of projects          | 9       | 26      | 21      |
| Value of overpayments (\$m) | 0.34    | 1.67    | 0.48    |
| Value of repayments (\$m)   | 0.34    | 0.72    | 0.40    |

Source: AusIndustry

### Variations to Agreements

**6.44** Grant recipients may request a variation to the terms and conditions of the Agreement,<sup>77</sup> including: increasing the project's duration (up to a maximum term of five years); increasing the amount of financial assistance (up to 30 per cent of the grant amount); changes to milestones; and changes to the control of the company and/or Intellectual Property.

<sup>76</sup> AusIndustry, *Customer Satisfaction Survey Report, R&D Start*, April 2004, p. 16.

<sup>77</sup> Part 11 of Ministerial Directions No. 3 of 2002 authorises the Board, on request of the recipient of a grant, to vary the terms of a Core Start, Start Plus or Start Graduate grant agreement, if the variation significantly advances the objectives of the project.

**6.45** Authority to approve most variations has been delegated by the Board to either the Financial Delegate, or the relevant State or Territory Manager. Authority to approve the change of control of a company and/or Intellectual Property to an overseas entity has not been delegated.<sup>78</sup> Approval controls are built into the grants management information system for most types of variations.

**6.46** Figure 6.5 outlines the number of variations requested by type of variation, and the proportion subsequently approved by the delegate. Most variations are requests to vary the length of the project. The delegate nearly always approves these requests.

**Figure 6.5**

**Agreement variations, 2001–02 to 2004–05**

| Type of variation                         | 2001–02      | 2002–03      | 2003–04     | 2004–05      | Total                |
|---|--------------|--------------|-------------|--------------|----------------------|
| Extension of time<br>(% approved)         | 166<br>(99%) | 160<br>(98%) | 98<br>(95%) | 73<br>(96%)  | <b>497<br/>(97%)</b> |
| Extension of funds<br>(% approved)        | 17<br>(82%)  | 12<br>(92%)  | 6<br>(67%)  | 2<br>(50%)   | <b>37<br/>(81%)</b>  |
| Extension of time & funds<br>(% approved) | 23<br>(100%) | 19<br>(79%)  | 19<br>(89%) | 18<br>(94%)  | <b>79<br/>(91%)</b>  |
| Changes to milestones<br>(% approved)     | 29<br>(100%) | 8<br>(100%)  | 9<br>(100%) | 11<br>(100%) | <b>57<br/>(100%)</b> |
| Non-extension variations<br>(% approved)  | 50<br>(94%)  | 38<br>(95%)  | 42<br>(90%) | 40<br>(95%)  | <b>170<br/>(93%)</b> |

Source: AusIndustry

Note: Non-extension variations include change of control of the company and/or transfers of Intellectual Property.

**6.47** The ANAO found that, in all but two variations examined,<sup>79</sup> the appropriate authority approved variations, with the required exchange of correspondence completed and recorded on the project file. In the two variations not appropriately authorised, no safeguard had been built into the grants management information system. Such a control measure would minimise the risk of incorrect variation approval of the type identified by the ANAO.

<sup>78</sup> The Board, or its delegate, must approve a change of control for up to five years after the completion of the grant.

<sup>79</sup> Variations were examined as part of the 2004–05 financial statements audit.

6.48 Approximately 75 per cent of instances of change of control reported by grant recipients in the biannual surveys were not approved by the Board, or its delegate. In June 2005, the Board clarified grant recipient obligations, under the Agreement, when a change of control is planned.<sup>80</sup> The policy states that the Board may terminate a grant Agreement, and seek up to 100 per cent repayment of the grant, if a change of control occurs without the Board's approval.

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Ian McPhee  
Auditor-General

Canberra ACT  
15 November 2005

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<sup>80</sup> Industry Research and Development Board, *Policy No. 15, Change in Control Policy*, June 2005, <<http://www.ausindustry.gov.au/content/content.cfm>> [accessed 3 August 2005].



# Appendices



## Appendix 1: Key responsibilities—R&D Start

Key responsibilities of Innovation Division and AusIndustry for the management and delivery of R&D Start are defined in a Business Partnership Agreement<sup>81</sup> between these two divisions of DITR. The key responsibilities are listed in Figure 1.

**Figure 1**

### Responsibilities for R&D Start specified in the Business Partnership Agreement

| Innovation Division  | AusIndustry   |
|--|---|
| <ul style="list-style-type: none"> <li>☐ Policy advice and briefings for the Minister</li> </ul>   | <ul style="list-style-type: none"> <li>☐ Interpret, for administrative purposes, current policy in consultation with Innovation Division</li> </ul>   |
| <ul style="list-style-type: none"> <li>☐ Develop and review policy options and obtain budgetary resources to achieve agreed outcomes of the program</li> </ul>   | <ul style="list-style-type: none"> <li>☐ Develop and implement the necessary materials, systems and standards to deliver the program</li> </ul>   |
| <ul style="list-style-type: none"> <li>☐ Undertake evaluations of appropriateness and effectiveness</li> </ul>   | <ul style="list-style-type: none"> <li>☐ Promote awareness and usage of the program to potential customers, efficiently deliver the program to customers within agreed standards, and be the first point of contact with customers</li> </ul> |
| <ul style="list-style-type: none"> <li>☐ Provide AusIndustry with information about, and consult with it on, any changes, or likely changes, to the program</li> </ul>   | <ul style="list-style-type: none"> <li>☐ Support policy development and monitoring by providing policy relevant feedback, access to data on the program, and recommendations on program design and effectiveness</li> </ul>                   |
| <ul style="list-style-type: none"> <li>☐ Interact with AusIndustry to develop and review performance indicators and assure that adequate and timely program performance information is being collected and analysed</li> </ul> |   |

Source: DITR

<sup>81</sup> Department of Industry, Tourism and Resources, *Business Partnership Agreement between Innovation Division and AusIndustry*.

## Appendix 2: Objectives of the 2004–05 National Marketing Strategy

The objectives of the 2004–05 National Marketing Strategy<sup>82</sup> were to:

- raise awareness of the Australian Government’s commitment to supporting business innovation to increase Australia’s competitiveness and attract investment;
- raise awareness of AusIndustry’s range of grants, tax concessions, venture capital and industry support products to stakeholders and potential customers;
- increase quality participation rates for AusIndustry products and services by target segments;
- raise awareness of the role played by AusIndustry as the business program delivery division of the Department and the Australian Government;
- increase AusIndustry brand and product awareness among target segments; and
- monitor and evaluate marketplace feedback mechanisms to identify issues, and inform ongoing marketing strategy and business development.

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<sup>82</sup> AusIndustry National Marketing Unit, *National Marketing Strategy 2004–2005*, August 2004.



## Appendix 3: Merit criteria

Applicants for a **Core Start** or **Start Plus** grant were required to present their case under five merit criteria:<sup>83</sup>

- **Management capability.** Applicants were required to provide details of the company's recent performance, examples of R&D undertaken and the technical and commercial results achieved, and the skills and experience of key personnel.
- **Commercial potential of the project.** Applicants were required to outline the work completed to determine the commercial potential of the project, the extent to which the project relied on access to patented intellectual property, and the products or services competing with the project's product or service.
- **Technical strength.** Applicants were required to provide a detailed project work plan that identified milestones and their capacity to undertake the project. Also, the project's technical risks and challenges were to be identified.
- **Level of National Benefit** the project would offer Australia, including Australian industry and the wider community. Applicants were required to outline benefits such as the impact on the Australian economy, employment, technology diffusion, environmental, health and other community benefits.
- **Need for R&D Start funding**—whether the project would proceed satisfactorily without financial assistance from the R&D Start program.

Applicants for a **Start Graduate** grant were required to present their case under four merit criteria:

- management capability;
- the extent to which projects to which applications relate would improve their performance through the adoption of appropriate technology or methodology;
- the extent to which projects form or strengthen appropriate links between them and research institutions; and
- whether the project would proceed satisfactorily without financial assistance from the R&D Start program.

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<sup>83</sup> The merit criteria for each type of financial assistance available under R&D Start were defined in the ministerial directions. (Commonwealth of Australia, *R&D Start Program Directions No. 3 of 2002*, 28 November 2002, Part 6.)

## Appendix 4: Committee appraisal procedures

The procedures used by committees to assess R&D Start applications are described below.

*Prior to the meeting:*

- Members reviewed, and rated, all applications on the agenda. This included an assessment of the strengths and weaknesses of the application, including a review of the project's milestones to ensure they were achievable and realistic.<sup>84</sup>
- Primary and secondary spokespersons for each application were appointed. These members reviewed the application in detail and prepared a short presentation on its strengths and weaknesses.

*At the meeting:*

- The nominated speakers presented their assessments on the application, and their individual merit ratings and total rating score.
- Other committee members advised their ratings, and discussed any differences they may have with the presented assessments. For example, at a meeting observed by the ANAO, a member had a different view of the financial assessment than the primary spokesperson, in particular the use of project expenditures to finance loans.
- All the members' ratings were aggregated, and an initial average total rating was calculated. Because this rating determined whether the application would be supported or rejected, members confirmed that the rating accorded with the committee's estimate of the application's level of competitiveness.
- If the rating accorded, the committee finalised its decision, including, if applicable, the identification of the reasons for the rejection.
- Most of the cases observed by the ANAO were in this category. The process of reaching a consensus on whether the rating accords sometimes entailed an open and extended discussion on the strengths and weaknesses of the application.
- Occasionally, the discussion compared the merits of the current application with the merits of previous applications or R&D projects known to the committee. For example, in one case, there was discussion on the capability of the applicant to undertake an R&D project that was

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<sup>84</sup> Members do not receive applications with which they have declared a conflict of interest.

similar to one that had been unsuccessfully undertaken by a large multi-national firm.

- If the rating did not accord, members discussed the initial average rating in the light of similar applications assessed in the past. This information and their qualitative assessments of this application after the discussion were used to agree a final rating.<sup>85</sup>
- In some cases, more information was sought to enable a final average rating to be agreed. For example, in one case observed by the ANAO, AusIndustry was asked to request more financial information from the applicant.
- After decisions have been made on all applications, the committee ranked the applications according to their overall merit. This ranking was to be used if insufficient funds were available to approve all supported applications across the four committees.

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<sup>85</sup> This comparison provides a measure of the application's merit (competitiveness) relative to the current and previous applications assessed by the committee.

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