

The Auditor-General  
Audit Report No.19 2007-08  
Performance Audit

## **Administration of the Automotive Competitiveness and Investment Scheme**

**Department of Innovation, Industry,  
Science and Research**

**Australian Customs Service**

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of Australia 2008

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Canberra ACT  
22 January 2008

Dear Mr President  
Dear Mr Speaker

The Australian National Audit Office has undertaken a performance audit in the Department of Innovation, Industry, Science and Research and Australian Customs Service 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 Automotive Competitiveness and Investment Scheme*.

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'.

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

The Auditor-General is head of the Australian National Audit Office. The ANAO assists the Auditor-General to carry out his duties under the *Auditor-General Act 1997* to undertake performance audits and financial statement audits of Commonwealth public sector bodies and to provide independent reports and advice for the Parliament, the Government and the community. The aim is to improve Commonwealth public sector administration and accountability.

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# Abbreviations

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ACIS	Automotive Competitiveness and Investment Scheme
ACPs	Automotive Component Producers
AMTPs	Automotive Machine Toolers / Automotive Tooling Producers
ANAO	Australian National Audit Office
ASIC	Australian Securities and Investment Commission
ASPs	Automotive Service Providers
Customs	Australian Customs Service
CSM	Customer Service Manager
DIISR	Department of Innovation, Industry, Science and Research
DITR	Department of Industry, Tourism and Resources (abolished on 3 December 2007)
ICN	Import Credit Number
ICS	Integrated Cargo System
IPMS	Integrated Program Management System
IR&D Board	Industry, Research and Development Board
MVPs	Motor Vehicle Producers
P&E	Plant and Equipment
R&D	Research and Development
The Scheme	The Automotive Competitiveness and Investment Scheme
TARCON	Tariff Concession System

# Glossary

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ACIS ledger	The official record of the import duty credits issued to Scheme participants. The ACIS ledger is kept in an electronic form within DIISR's Integrated Program Management System.
ACIS quarter	A period of three months commencing on 1 January, 1 April, 1 July or 1 October of an ACIS year.
ACIS year	The year commencing on the scheme commencement date (1 January 2001) and each succeeding year, before the year commencing 1 January 2016.
Automotive component	Any component that is for use in any type of vehicle that, if imported, would be classified under Chapter 87 of Schedule 3 to the <i>Customs Tariff Act 1995</i> , other than a component of a kind that is declared by the ACIS Administration Regulations 2000 not to be an automotive component.
Automotive machine tool	A machine tool designed and built to be used solely for the production of motor vehicles, engines, engine components or automotive components, or facilitating the provision of automotive services.
Eligible imports	Prescribed goods to which ACIS duty credits can be applied to reduce the import duty payable.
Import duty credits	Earned by participants for the production of motor vehicles and investment in plant and equipment or in research and development. Each credit has a nominal value of one Australian dollar. Credits can be used to offset the duty on certain imports (motor vehicles and related parts) or can be sold to other Scheme participants or to third-parties.
Modulation	The process of limiting ACIS credits in the capped pool to \$2 billion over the five years of Stage 2.



Registered participant	An entity registered under ACIS as a motor vehicle producer, automotive component producer, automotive machine tooler, automotive tooling producer or an automotive service provider, who earns duty credits.
Ledger participant	An entity that is not registered under ACIS, and does not earn duty credits, but has an account in the ACIS ledger to purchase and trade duty credits.
Quarterly returns	A claim form submitted by a registered participant setting out the particulars of the participant's production and / or expenditure claims for the quarter in which a claim is made.
Tariff	The percentage of customs duty payable on imported goods.
The Act	The <i>ACIS Administration Act 1999</i> .
The department	The Department of Innovation, Industry, Science and Research.
The Minister	The Minister responsible for administering the <i>ACIS Administration Act 1999</i> , currently the Minister for Innovation, Industry, Science and Research.
The Regulations	The ACIS Administration Regulations 2000.



# Summary and Recommendations



# Summary

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## Introduction

1. Although small by world standards, the automotive industry is one of Australia's major manufacturing sectors.<sup>1</sup> In 2006–07, it generated \$4.7 billion in export revenue and employs around 80 000 people.<sup>2</sup> The industry is particularly important to the economies of Victoria and South Australia, where the major motor vehicle manufacturing facilities and automotive supply chain companies are concentrated.

2. Globally, the automotive industry is being transformed and realigned in the context of emerging markets, such as China and India, freer trade and changing consumer preferences.<sup>3</sup> These changes are impacting on various parts of the industry, including in Australia.

3. The Automotive Competitiveness and Investment Scheme (ACIS) was established in 2001 as part of the Australian Government's post-2000 assistance package for the automotive industry.<sup>4</sup> The purpose of the Scheme is to provide:

... transitional assistance to encourage competitive investment and innovation in the Australian automotive industry in order to achieve sustainable growth, both in the Australian market and internationally, in the context of trade liberalisation.<sup>5</sup>

4. ACIS is open to Australia's motor vehicle producers (MVPs)—Ford, Holden, Mitsubishi and Toyota—and to companies operating within the automotive supply chain including: automotive component producers (ACPs); automotive machine tooling producers (AMTPs); and automotive service providers (ASPs). At 30 June 2007, there were 245 participants registered under the Scheme.

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<sup>1</sup> Australia manufactures around 330 000 motor vehicles annually, some 0.5 per cent of world production.

<sup>2</sup> Department of Industry, Tourism and Resources, Automotive Industry Policy Fact Sheet, 2007 [Internet], available from <<http://www.industry.gov.au>> [accessed 16 October 2007].

<sup>3</sup> See KPMG, *Momentum 2007 KPMG Global Auto Executive Survey*, KPMG, Munich, 2007.

<sup>4</sup> Other parts of the package include the now defunct Automotive Market Access and Development Strategy, and changes to the tariff regime for motor vehicles.

<sup>5</sup> Section 3 of the *ACIS Administration Act 1999*.

5. Once registered, participants are able to earn import duty credits for investing in plant and equipment (P&E) and in research and development (R&D). MVPs are also able to earn credits for producing motor vehicles. Duty credits have a nominal value of one Australian dollar, and can be used to offset the duty payable on certain imports (motor vehicles and related parts) or traded with other Scheme participants and third-parties.<sup>6</sup> The benefits to individual entities under ACIS have so far ranged from tens of thousands of duty credits to, in some cases, hundreds of millions of duty credits.

6. ACIS was originally established to run for a five-year period until 31 December 2005. In December 2002, the Government announced a ten-year extension to the Scheme, comprising two five-year stages. Stage 2 of the Scheme commenced on 1 January 2006 and runs until 31 December 2010, while Stage 3 commences on 1 January 2011 and concludes on 31 December 2015. Up to \$7 billion worth of duty credits are expected to be provided to participants over the 15 years of the Scheme.

7. In Stage 2, there are two funding pools from which duty credits are issued—a \$2 billion capped pool and an uncapped pool. MVPs are entitled to claim \$1.1 billion (or 55 per cent) of the capped pool, with the balance available to supply chain participants. The uncapped pool is available only to MVPs and is expected to cost around \$800 million in Stage 2.

8. The major change from Stage 1 to Stage 2 was the introduction of the \$150 million Motor Vehicle Producer Research and Development (MVP R&D) Scheme. This Scheme provides funding to MVPs on a competitive basis, and is directed at encouraging investment in 'high-end' R&D technologies.

## **Administrative arrangements**

9. The Department of Innovation, Industry, Science and Research (DIISR) is responsible for administering ACIS under the *ACIS Administration Act 1999* (the Act) and accompanying regulations.<sup>7</sup> The Australian Customs Service (Customs) also delivers aspects of the Scheme, under its separate legislation.<sup>8</sup> Broadly, the agencies' responsibilities are as follows:

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<sup>6</sup> The trading of duty credits allows participants who do not import eligible goods to obtain a financial benefit from ACIS by selling their duty credits to other parties.

<sup>7</sup> This department was established following the election of the Labor government in November 2007. Previously, ACIS was administered by the Department of Industry, Tourism and Resources.

<sup>8</sup> Customs undertakes its functions under the *Customs Tariff Act 1995* and accompanying regulations.

- AusIndustry, a division within DIISR, is responsible for the day-to-day delivery of the Scheme. This includes registering applicants, issuing duty credits to participants and transferring credits to Customs, to be used on eligible imports; and
- Customs is responsible for facilitating the use of duty credits on eligible imports and for reporting to DIISR on the use of those credits.

10. To receive duty credits, participants are required to submit a claim form to DIISR each quarter detailing their investment in P&E, R&D and, for MVPs, the production of motor vehicles. The department issues duty credits to participants once the claim is received, and subsequently checks the integrity of claims. DIISR's principal means of identifying mis-claiming are by conducting compliance audits on selected participants, and by using ACIS customer service managers (CSMs) to review participants' quarterly claim forms. CSMs may also verify some aspects of participants' claims during site visits to participants' premises. For example, confirming that capital equipment previously claimed exists and is allowable under the Regulations.

## Audit objective and scope

11. The ANAO undertook a previous audit of ACIS in 2002–03 during Stage 1 of the Scheme. The audit made six recommendations to improve the department's management of the Scheme covering aspects of governance, performance reporting and risk management arrangements.<sup>9</sup>

12. The current audit has focussed on Stage 2 of the Scheme. Its objective was to assess whether ACIS is being administered effectively by DIISR and, as relevant, by Customs. In particular, the audit examined the department's arrangements for:

- assessing the eligibility of participants to receive duty credits;
- calculating duty credits accurately and adhering to the funding limits for the Scheme;
- checking the integrity of participants' claims, which are self-assessed;
- accounting for the duty credits transferred to and used at Customs; and
- measuring and reporting on the performance of ACIS.

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<sup>9</sup> Australian National Audit Office Audit Report No.63 2002–03 *Administration of the Automotive Competitiveness and Investment Scheme*, pp. 21–24.

13. The audit also followed up on whether the ANAO's previous recommendations have been addressed. These recommendations are covered in the body of the report and are summarised in Appendix 2.

## Conclusion

14. ACIS is the Australian Government's key measure for supporting the automotive industry. As at July 2007, more than \$3.4 billion in duty credits have been issued to eligible companies from the automotive industry since the Scheme began in 2001. In 2004, the department assessed whether the stated objectives of the Scheme were being achieved, and early indications were that ACIS was helping to promote a more competitive and sustainable automotive industry in Australia. DIISR plans to evaluate the performance of ACIS again in 2009, one year before the end of Stage 2. As well, the Productivity Commission is scheduled to review government assistance to the automotive sector in 2008. ACIS is legislated to run until 2015.

15. In its administration of the Scheme, DIISR has implemented effective internal controls to assess the eligibility of participants to receive credits; to calculate duty credits claims accurately, based on the information provided by participants; and to adhere to the funding limits for the Scheme. DIISR has also established appropriate arrangements for managing the \$150 million MVP R&D Scheme introduced in Stage 2.

16. Since DIISR administers ACIS on a 'self-assessment' basis, it requires effective arrangements to promote accurate claiming and to identify any mis-claiming by participants. Compliance activities have identified some \$141 million in inappropriate claiming since 2001. The department uses various methods to educate participants on Scheme requirements, and it conducts risk-based compliance audits to check whether self-assessed claims are accurate. These audits have covered all of the largest recipients of duty credits. However, most participants have been audited only once since ACIS began in 2001. While it is a matter of judgement where the appropriate balance lies, the level of audit coverage is relatively light for such a significant program that operates on a 'self-assessment' basis.

17. To further strengthen its compliance program, there is an opportunity for DIISR to systematically analyse, and use, the results from its compliance activities to improve participants' understanding of Scheme requirements. Such analysis could also be used to better inform DIISR's approach to determining the coverage and scope of compliance audits. Audits with a



stronger focus on high risk areas are likely to be more cost-effective, providing capacity to increase the extent of coverage.

18. DIISR has established a ledger to record the number of duty credits held by Scheme participants, and Customs has a sound control framework to ensure that duty credits which are transferred from DIISR to Customs are used only on eligible imports. However, the department's processes to account for transferred duty credits have not been sufficiently robust in recent years. This has impacted on its ability to identify errors in participants' duty credit accounts, and to report accurately on ACIS, including in its financial statements. A more comprehensive reconciliation process is now being put in place between DIISR and Customs.

19. DIISR collects performance data on the Scheme's intermediate outcomes and annual outputs. However, little information has been reported publicly for the benefit of external stakeholders, including the Parliament. The department has concerns about the commercial sensitivities involved in reporting publicly on aspects of ACIS, particularly the number of duty credits issued to *individual* participants. However, given that ACIS is the Australian Government's key assistance measure for the automotive industry and involves a substantial amount of government support, there is scope to provide greater disclosure of the duty credits issued to Scheme participants.

20. The ANAO has made three recommendations aimed at improving the administration of ACIS, and to ensure that aspects of the ANAO's previous recommendations are fully implemented.

## Key findings

### Issuing ACIS duty credits (Chapter 2)

21. In Stage 2, around \$2.8 billion in duty credits are expected to be issued to participants. The Act prescribes who is eligible to earn duty credits, how duty credits are to be calculated and overall funding limits for the Scheme. DIISR has established a sound control framework to comply with legislative requirements and to manage financial risks when issuing duty credits. It has well-developed processes to assess the eligibility of participants to receive credits; to calculate individual duty credits claims accurately, based on the information provided by participants; and to adhere to the funding limits for the Scheme.

22. DIISR's key mechanism for adhering to the \$2 billion funding cap for Stage 2 (as with Stage 1) is by setting a modulation rate to reduce participants' claims, where those claims are forecast to exceed the available credits. In Stage 2 the modulation rate has fluctuated between 0.70 and 0.62 for MVPs, and between 0.71 and 0.63 for supply chain companies. In Stage 1, the \$2 billion capped funding limit was not exceeded, and some 99 per cent of available duty credits were issued.

23. DIISR has also implemented appropriate processes to manage the allocation of credits under the \$150 million MVP R&D Scheme introduced in Stage 2. This includes monitoring whether participants are complying with the requirements of their funding agreements, and taking appropriate actions when these requirements have not been met.

### **Claims made by Scheme participants (Chapter 3)**

24. DIISR administers ACIS on a 'self-assessment' basis. Participants determine what they are entitled to claim under the Scheme, and DIISR issues duty credits based on their quarterly claims. This approach allows duty credits to be provided on a timely basis. It also means that DIISR needs to manage the risk of mis-claiming, to ensure that duty credits are issued appropriately and equitably.

25. Since ACIS began on 1 January 2001, DIISR has identified some \$141 million in ineligible activities claimed by participants. Compliance audits undertaken at participants' premises are DIISR's best tool for identifying mis-claiming. These audits have been focussed on those participants DIISR considers to be high and medium risk, and who receive the vast majority of duty credits. However, most participants have been audited only once in the six years since ACIS began. In practice, this means that DIISR relies to a large degree on the voluntary compliance of participants.

26. DIISR uses various methods to assist participants to lodge accurate claims. This includes publishing customer guidelines on various aspects of the Scheme, and assigning a customer service manager to each participant. Notwithstanding these measures, the level of mis-claiming identified to date suggests that further efforts are needed in this area. In particular, DIISR has yet to systematically analyse, and use, the findings from its compliance activities to improve participants' understanding of Scheme requirements. The ANAO's analysis of 20 completed audit files indicated that more targeted guidance material for participants is likely to reduce some of the mis-claiming that is

occurring. Such an approach would also address a concern of participants, which is that the department should be more proactive in providing guidance on activities able to be claimed under ACIS.

27. Systematic analysis of the results from compliance activities could also be used to better inform DIISR's approach to determining the coverage and scope of compliance audits. For example, where analysis indicates a higher level of mis-claiming in certain activities (for instance, offshore R&D), compliance audits could focus on this specific issue, rather than attempting to examine all aspects of a claim, as currently happens. Audits with a stronger focus on high risk areas are likely to be more cost-effective, providing capacity to increase the extent of coverage.

### **Use of ACIS duty credits (Chapter 4)**

28. Since ACIS began in 2001, more than \$3.4 billion in duty credits have been transferred from DIISR to Customs, to be used to offset the duty payable on eligible imports or to obtain a refund for duty previously paid.

29. DIISR has established a ledger to record the number of duty credits held by Scheme participants, and Customs has a sound control framework to ensure that transferred duty credits are used only on eligible imports.<sup>10</sup> However, the agencies have experienced difficulties in reconciling their records on the duty credits transferred to and used at Customs. For example, at 30 June 2006, there was a variance of around \$136 million between the expected balance of unused duty credits at Customs, and the balance reported by Customs.<sup>11</sup> In recent years, the absence of a more robust reconciliation process has affected the department's ability to report accurately on ACIS for financial statement purposes, and to provide assurance that participants have not used more credits at Customs than were originally issued by DIISR.

### **Effectiveness of the Scheme (Chapter 5)**

30. ACIS is a transitional assistance scheme intended to assist the automotive industry to adjust to a lower tariff environment. In 2004, DIISR assessed whether the Scheme was meeting its stated objectives and early indications were that the Scheme is assisting the industry to become more

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<sup>10</sup> These include certain motor vehicles for the transportation of passengers and goods, including used and second-hand vehicles, and certain components for those vehicles.

<sup>11</sup> Of this amount, some \$122 million was subsequently found to relate to an inaccurate balance provided by Customs for one Scheme participant.

competitive and sustainable. Also, the high demand for duty credits in Stage 1 and Stage 2 (to date) suggests that the Scheme has been effectively promoted within the automotive industry. DIISR plans to evaluate the performance of ACIS again in 2009, one year before the end of Stage 2. As well, the Productivity Commission is scheduled to review government assistance to the automotive sector in 2008.

31. Although DIISR collects performance data on intermediate outcomes and annual outputs, only limited information has been reported publicly for the benefit of external stakeholders, including the Parliament. The ANAO recognises that the department has concerns about the commercial sensitivities involved in publicly disclosing aspects of the Scheme, including the number of duty credits issued to *individual* participants. However, the absence of performance information has limited the transparency of ACIS, which is the Government's key assistance measure for the automotive industry.

## Summary of DIISR and Customs' response to this audit

### DIISR

32. The department notes the ANAO's conclusion that it has established a sound control framework to facilitate compliance with legislative requirements and to manage financial risks when issuing credits in the ACIS scheme. In addition the ANAO has indicated that the department has well-developed processes in place to assess the eligibility of scheme participants to receive credits and to accurately calculate individual claims while ensuring adherence to the funding limits of the scheme. Further, the ANAO has found that the department has implemented appropriate processes to manage the allocation of credits under the \$150 million MVP R&D Scheme. The department accepts the recommendation to provide more public reporting; the recommendation to enhance its targeting of compliance actions and the recommendation to upgrade its credit reconciliation process with Customs.

### Customs

33. Customs notes the ANAO finding that Customs has a sound framework to manage the use of ACIS credits for eligible imports. Similarly, the ANAO found that Customs' controls over the payment of ACIS refunds, and refunds generally, are satisfactory.

34. Customs recognises the need to update and further develop procedural documentation with DIISR to ensure that the responsibilities of each agency are more clearly defined.

35. DIISR and Customs' full response to the audit can be found at Appendix 1.

# Recommendations

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Set out below are the ANAO's three recommendations for improving DIISR and Customs' administration of ACIS. Paragraph references and the agencies' summary response to each recommendation are also provided.

**Recommendation No. 1** The ANAO recommends that the Department of Innovation, Industry, Science and Research

**Para 3.29** systematically analyse and use the results of compliance activities of the Automotive Competitiveness and Investment Scheme to:

- (a) inform its approach to promoting accurate claiming by Scheme participants; and
- (b) determine the coverage and scope of future compliance audits.

*DIISR response:* Agreed.

**Recommendation No. 2** The ANAO recommends that the Department of Innovation, Industry, Science and Research and the

**Para 4.31** Australian Customs Service review their governance arrangements, and document procedures, to support their respective responsibilities for managing the transfer, use and reporting of duty credits under the Automotive Competitiveness and Investment Scheme.

*DIISR response:* Agreed.

*Customs response:* Agreed.

**Recommendation  
No. 3****Para 5.20**

The ANAO recommends that the Department of Innovation, Industry, Science and Research enhance the level of public reporting on the Automotive Competitiveness and Investment Scheme, including:

- (a) the aggregate number of duty credits issued to motor vehicle producers and the three supply chain sectors;
- (b) the broad results of compliance activities; and
- (c) progress against intermediate outcomes, as data becomes available.

*DIISR response:* Agreed.





# **Audit Findings and Conclusions**



# 1. Background and Context

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*This chapter provides information on the Australian automotive industry and describes the assistance provided under ACIS. The objective, scope and methodology of the audit are also outlined.*

## The Australian automotive industry

1.1 Although small by world standards, the automotive industry is one of Australia's major manufacturing sectors, specialising in the production of large, four and six-cylinder passenger vehicles (see example in Figure 1.1).<sup>12</sup> In 2004–05, the industry accounted for approximately 0.7 per cent of gross domestic product, some \$6 billion<sup>13</sup>; while in 2006–07 it generated over \$4.7 billion in export revenue. More than 80 000 people are employed within the industry.<sup>14</sup>

**Figure 1.1**

### Production of the Toyota Camry in Victoria, Australia



Source: Federation of Automotive Products Manufacturers

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<sup>12</sup> Australia manufactures around 330 000 motor vehicles annually, some 0.5 per cent of world production.

<sup>13</sup> Australian Bureau of Statistics, Year Book Australia 2005 [Internet], available from <<http://www.abs.gov.au>> [accessed 20 August 2007].

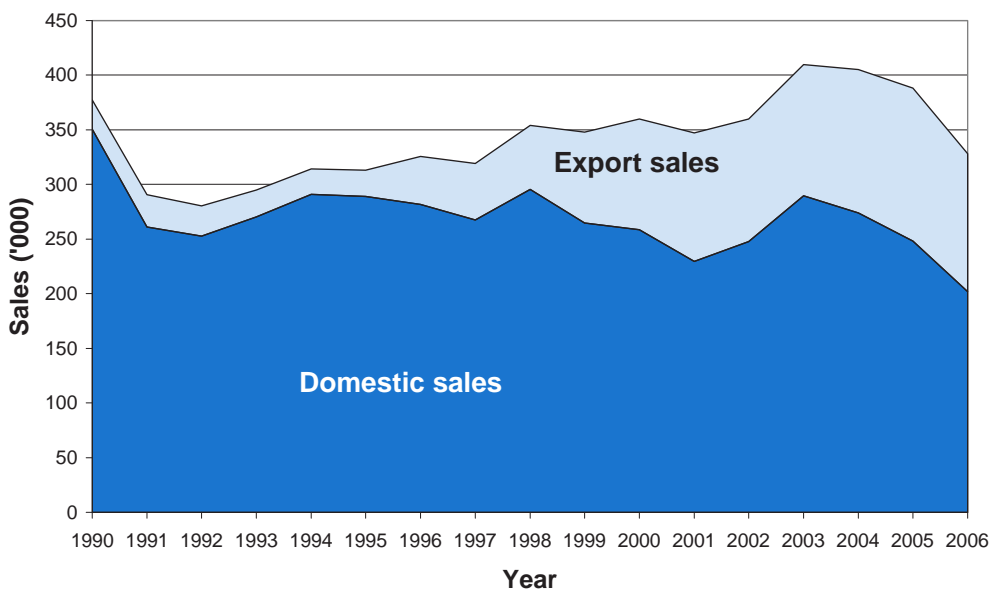
<sup>14</sup> Department of Industry, Tourism and Resources, *Automotive Industry Policy Fact Sheet, 2007* [Internet], available from <<http://www.industry.gov.au>> [accessed 16 October 2007].

1.2 The industry is comprised of four motor vehicle producers (MVPs)—Ford, Holden, Mitsubishi and Toyota—and over 200 entities operating within the automotive supply chain. These entities include component, tooling, design engineering and service companies. All four MVPs and many of the supply chain entities are subsidiaries of overseas companies. The industry is particularly important to the economies of Victoria and South Australia, where the major manufacturing facilities and supply chain companies are based.

1.3 Over the last three years, total sales of Australian-made vehicles have declined due to a reduction in domestic sales. This reduction has been attributed, in part, to changing consumer preferences away from large cars to smaller, more fuel-efficient vehicles. However, exports of Australian-made vehicles have steadily increased and now represent approximately one-third of all vehicles sold, as illustrated in Figure 1.2.

**Figure 1.2**

**Sales of Australian-made motor vehicles, between 1990 and 2006**



Source: Department of Innovation, Industry, Science and Research

1.4 Like other manufacturing industries, the automotive industry is susceptible to changes in the exchange rate. For example, the recent strengthening of the Australian dollar against other currencies, especially the United States dollar, has made imported vehicles more affordable. But, a

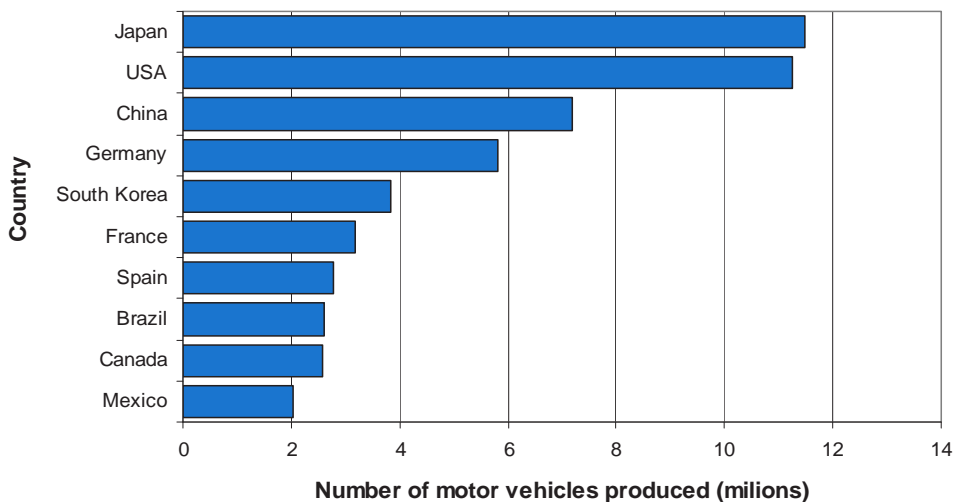
stronger dollar also makes Australian-made motor vehicles relatively more expensive to other countries, potentially affecting export sales.

## International context

1.5 Internationally, the demand for motor vehicles is increasing, particularly in growing markets like China, India and Vietnam. In 2006, China overtook Germany as the third-largest producer of motor vehicles.<sup>15</sup> The top ten motor vehicle producing countries in 2006 are shown in Figure 1.3. Yet, despite rising demand, there is global overcapacity of production, which has resulted in financial difficulties and low profitability across parts of the industry worldwide.<sup>16</sup>

**Figure 1.3**

### Top ten motor vehicle producing countries, 2006



Source: International Organisation of Motor Vehicle Manufacturers<sup>17</sup>

1.6 The automotive industry is becoming more open under bilateral, regional and global trade agreements.<sup>18</sup> For example, Australia has signed free trade agreements with Thailand and the United States of America. The

<sup>15</sup> International Organisation of Motor Vehicle Manufactures, 2006 production statistics [Internet], available from <[http://oica.net/category/production-statistics, 2006](http://oica.net/category/production-statistics,2006)> [accessed on 11 October 2007].

<sup>16</sup> KPMG, *Momentum 2007 KPMG Global Auto Executive Survey*, KPMG, Munich, 2007, p 7.

<sup>17</sup> International Organisation of Motor Vehicle Manufactures, op. cit.

<sup>18</sup> The Australian APEC Study Centre, *An Australia—USA Free Trade Agreement: Issues and Implications*, Department of Foreign Affairs and Trade, 2001, Canberra, p. 104.

agreements reduce the tariffs on automotive products both in Australia and in these countries. However, domestic automotive industries typically receive strong government support. This support can include import tariffs, quotas and other restrictions, and budgetary assistance through direct grants and export assistance schemes.

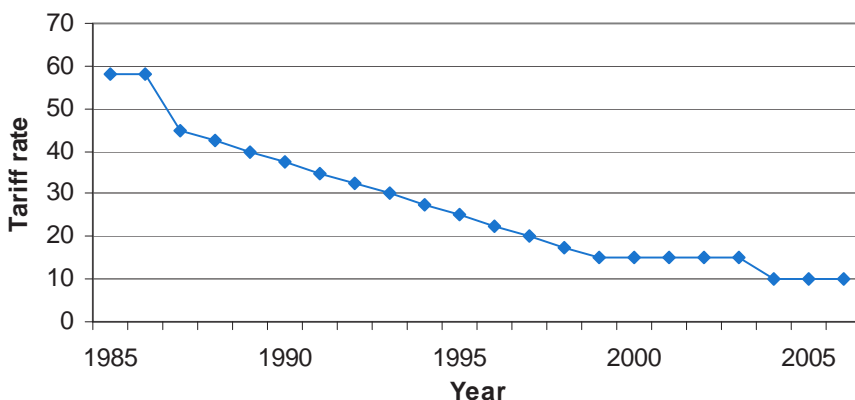
### Government assistance

1.7 The Australian Government supports the automotive industry through various measures including tariffs on imported motor vehicles, direct financial grants<sup>19</sup> and import duty concessions. The industry also has access to a range of generally available support measures, such as research and development grants and tax concessions. As well, the industry receives ad hoc support from State governments via payroll tax concessions, grants and low interest loans.<sup>20</sup>

1.8 As illustrated in Figure 1.4, tariff rates on passenger motor vehicles have declined steadily over the past 20 years. Moreover, tariffs are scheduled to fall from ten to five per cent by 2010.

**Figure 1.4**

**Tariff rates on passenger motor vehicles, between 1985 and 2007**



Source: Department of Innovation, Industry, Science and Research

<sup>19</sup> For example, in 2005–06 the Government committed to \$52.5 million in assistance to the Ford Motor Company of Australia, which will assist: the design, engineering and manufacture of the next Ford Falcon and Ford Territory; and the design and engineering of a light commercial vehicle to be manufactured in Thailand and sold worldwide.

<sup>20</sup> Productivity Commission Report No.25, 30 August 2002, *Review of Automotive Assistance*, p.XVIII.

1.9 Despite the reduction in tariffs, the automotive industry remains one of Australia's most highly assisted and protected manufacturing industries.<sup>21</sup> Approximately one-third of all budgetary funding provided to the manufacturing sector goes to the automotive industry. The Government's key assistance measure for the industry is the Automotive Competitiveness and Investment Scheme (ACIS), which is the subject of this audit.

## Automotive Competitiveness and Investment Scheme

1.10 ACIS was established on 1 January 2001 as part of the Australian Government's post-2000 assistance package for the automotive industry. The purpose of the Scheme is to provide:

... transitional assistance to encourage competitive investment and innovation in the Australian automotive industry in order to achieve sustainable growth, both in the Australian market and internationally, in the context of trade liberalisation.<sup>22</sup>

1.11 The Scheme is open to MVPs and to companies operating within the automotive supply chain including: automotive component producers (ACPs); automotive machine tooling producers (AMTPs); and automotive service providers (ASPs).

1.12 To be eligible to register under ACIS, companies have to meet eligibility criteria in relation to the volume or value of production in Australia (as outlined in Table 2.1). For example, MVPs have to produce at least 30 000 vehicles or engines annually. Once registered, participants are able to earn import duty credits for investing in plant and equipment (P&E) and in research and development (R&D). MVPs are also able to earn credits for producing motor vehicles. These benefits are outlined in Table 1.1.

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<sup>21</sup> Productivity Commission, *Trade and Assistance review 2005–06*, PC, 2007, p. 3.16.

<sup>22</sup> Section 3 of the *ACIS Administration Act 1999*.

**Table 1.1**

**Eligible activities and benefits under ACIS (Stage 2)**

Type of participant	Eligible activity	Benefits
<b>Motor vehicle producers</b>	Production of motor vehicles sold in Australia and New Zealand	<ul style="list-style-type: none"> <li>• 10 per cent of production value multiplied by the automotive tariff rate; and</li> <li>• 15 per cent of production value multiplied by the automotive tariff rate<sup>23</sup></li> </ul>
	Production of motor vehicles sold overseas (except New Zealand)	<ul style="list-style-type: none"> <li>• 25 per cent of production value, multiplied by the automotive tariff rate</li> </ul>
	Investment in plant and equipment	<ul style="list-style-type: none"> <li>• 10 per cent of the value of investment.</li> <li>• 25 per cent of the value of the investment, for non-own use</li> </ul>
	Investment in research and development	<ul style="list-style-type: none"> <li>• 45 cents for every dollar spent on eligible R&amp;D under the MVP R&amp;D Scheme</li> <li>• 45 per cent of the value of the investment, for non-own use</li> </ul>
<b>Supply chain entity</b>	Investment in research and development	<ul style="list-style-type: none"> <li>• 45 per cent of the value of investment</li> </ul>
	Investment in plant and equipment	<ul style="list-style-type: none"> <li>• 25 per cent of the value of investment</li> </ul>

Source: ANAO analysis based on the *ACIS Administration Act 1999*

1.13 ACIS duty credits represent revenue foregone on customs duty payable, and have a nominal value of one Australian dollar. They can be used to offset the duty on certain imports (motor vehicles and related parts) or can be sold to other Scheme participants or to third-parties, such as companies that import motor vehicles.<sup>24</sup>

1.14 ACIS was originally established to run for a five-year period until 31 December 2005. In December 2002, the Government announced a ten-year extension to the Scheme, comprising two five-year stages. Stage 2 of the Scheme commenced on 1 January 2006 and runs until 31 December 2010, while Stage 3 commences on 1 January 2011 and concludes on 31 December 2015. Up to \$7 billion worth of duty credits are expected to be provided to participants over the 15 years of the Scheme.

<sup>23</sup> This is the only benefit funded from the uncapped funding pool, not the \$2 billion capped pool.

<sup>24</sup> The trading of duty credits allows participants who do not import eligible goods to obtain a financial benefit from ACIS by selling their duty credits to other parties.



1.15 In Stage 2, there are two funding pools from which duty credits are issued—a \$2 billion capped pool and an uncapped pool. MVPs are entitled to claim \$1.1 billion (or 55 per cent) of the capped pool, with the balance available for supply chain participants. The uncapped pool is available only to MVPs and is expected to cost around \$800 million in Stage 2.

1.16 The major change from Stage 1 to Stage 2 was the introduction of the \$150 million Motor Vehicle Producer Research and Development (MVP R&D) Scheme. This Scheme provides funding to MVPs on a competitive basis, and is directed at encouraging investment in ‘high-end’ R&D technologies.

## Legislative and administrative framework

1.17 The Department of Innovation, Industry, Science and Research (DIISR) is responsible for administering ACIS under the *ACIS Administration Act 1999* (the Act) and accompanying regulations.<sup>25</sup> The Australian Customs Service (Customs) is also involved in delivering aspects of the Scheme, under its separate legislation.<sup>26</sup> Broadly, the agencies’ responsibilities are as follows:

- AusIndustry, a division within DIISR, is responsible for the day-to-day delivery of the Scheme. This includes registering applicants, issuing duty credits to participants and transferring credits to Customs, to be used on eligible imports; and
- Customs is responsible for facilitating the use of duty credits on eligible imports, and reporting to DIISR on the use of those credits.

1.18 DIISR and Customs’ roles and responsibilities for administering ACIS are managed, at a high level, through a Memorandum of Understanding (MoU) that was formally signed in July 2003.<sup>27</sup>

## Processing participants’ claims

1.19 To receive duty credits, participants are required to submit a claim form to DIISR each quarter detailing their investment in P&E, R&D and, for MVPs, the production of motor vehicles. DIISR administers ACIS on a ‘self-assessment’ basis, whereby it issues duty credits to participants when

<sup>25</sup> This department was established following the election of the Labor government in November 2007. Previously, ACIS was administered by the Department of Industry, Tourism and Resources.

<sup>26</sup> Customs undertakes its functions under the *Customs Tariff Act 1995* and accompanying regulations.

<sup>27</sup> The MoU was in ‘draft’ during the ANAO’s previous audit of ACIS. Its finalisation has addressed part of Recommendation No. 1 from Australian National Audit Office Audit Report No.63 2002–2003 *Administration of the Automotive Competitiveness and Investment Scheme*, p. 36.

quarterly claim forms are received, and then checks the integrity of claims. DIISR's principal means of identifying mis-claiming are by conducting compliance audits on selected participants, and by using ACIS customer service managers (CSMs) to review participants' quarterly claim forms. CSMs may also verify some aspects of participants' claims during site visits to participants' premises (which occur separately to compliance audits). For example, confirming that capital equipment previously claimed exists, and is allowable under the Regulations.

1.20 Participants found to have claimed duty credits inappropriately are required to repay the credits, either by offsetting the debt against other credits earned, or by repaying the debt through DIISR's normal debt management process.

## **Audit objective, scope and methodology**

1.21 The ANAO undertook a previous audit of ACIS in 2002–03 during Stage 1 of the Scheme. The audit made six recommendations to improve the department's management of the Scheme, covering aspects of governance, performance reporting and risk management arrangements.<sup>28</sup>

1.22 The current audit has focussed on Stage 2 of the Scheme. Its objective was to assess whether ACIS is being administered effectively by DIISR and, as relevant, by Customs. In particular, the audit examined the department's arrangements for:

- assessing the eligibility of participants to receive duty credits;
- calculating duty credits accurately and adhering to the funding limits for the Scheme;
- checking the integrity of participants' claims, which are self-assessed;
- accounting for the duty credits transferred to and used at Customs; and
- measuring and reporting on the performance of ACIS.

1.23 The audit also followed up on whether the ANAO's previous recommendations have been addressed. These recommendations are covered in the body of the report, and are summarised in Appendix 2.

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<sup>28</sup> ANAO, *op. cit.*, pp. 21–24.

## Audit methodology

1.24 The audit methodology included: quantitative and qualitative analysis of agency data; examination of agency documentation and files; interviews with officers from DIISR and Customs; and discussions with ACIS participants and industry stakeholders.

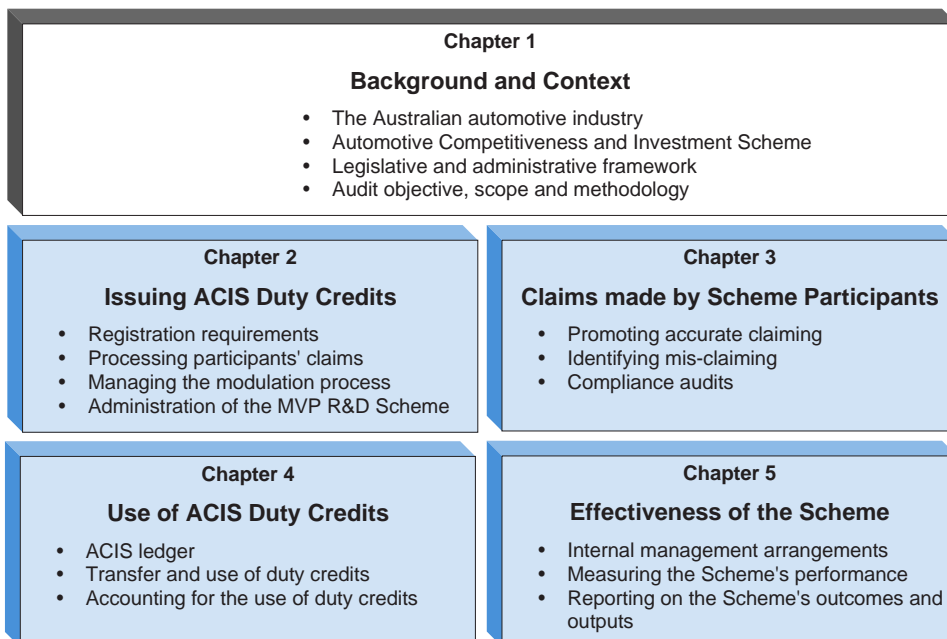
1.25 The audit was conducted in accordance with ANAO auditing standards, and cost \$350 000.

## Report structure

1.26 The structure for this report is outlined in Figure 1.5.

**Figure 1.5**

### Report structure



## 2. Issuing ACIS Duty Credits

*This chapter examines whether ACIS duty credits are calculated accurately, allocated within required funding limits and issued only to eligible entities.*

### Introduction

2.1 During ACIS Stage 2, it is anticipated that around \$2.8 billion in duty credits will be issued to the Scheme's participants. The Act prescribes who is eligible to earn duty credits, how credits are to be calculated and the overall funding limits for the Scheme.

2.2 The ANAO assessed whether DIISR has established sound processes to comply with legislative requirements and to manage the financial risks associated with issuing duty credits. This includes those credits issued under the \$150 million MVP R&D Scheme, introduced in Stage 2.

### Registration requirements

2.3 To be eligible to register under ACIS, and to remain registered in each subsequent year, companies have to meet eligibility criteria in relation to the volume or value of production in Australia, as outlined in Table 2.1.

**Table 2.1**

#### Production criteria for initial and ongoing registration under ACIS

Registration category	Eligibility requirements
Motor vehicle producers	<ul style="list-style-type: none"><li>• Must produce at least 30 000 motor vehicles or 30 000 engines annually.</li></ul>
Automotive component producers	<ul style="list-style-type: none"><li>• Must produce at least \$500 000 of one kind of automotive component annually for use as original equipment in at least 30 000 motor vehicles or 30 000 engines; or</li><li>• Manufacture at least \$500 000 of original equipment components annually, where that production represents at least 50 per cent of the total value of a producer's automotive component production.</li></ul>
Automotive machine tool or automotive tooling producers	<ul style="list-style-type: none"><li>• Must produce at least \$500 000 of automotive machine tools or automotive tooling annually, where at least 50 per cent of that production is used to produce original equipment.</li></ul>
Automotive service providers	<ul style="list-style-type: none"><li>• Must produce at least \$500 000 of automotive services annually, where at least 50 per cent of those services relate to the production of motor vehicles or original equipment.</li></ul>

Source: *ACIS Administration Act 1999*

2.4 Applicants must also satisfy other registration requirements including:

- being a 'fit and proper person' within the meaning of the Act<sup>29</sup>;
- being able to comply with the document retention obligations set out in the Act; and
- providing an annual business plan forecasting expenditure on eligible activities under the Scheme.

2.5 Companies that are unable to meet the production criteria in Table 2.1 can apply to the Minister for Innovation, Industry, Science and Research for permission to register under ACIS for reasons of national interest.<sup>30</sup> DIISR advised the ANAO that there have been eight such applications since the beginning of the Scheme, one of which, an MVP, was given permission to register under this provision in July 2004.

2.6 At 30 June 2007, there were 245 participants registered under Stage 2, including the national interest registration. Of these participants, 20 new companies have been registered since the start of Stage 2, all from the automotive supply chain.<sup>31</sup> All remaining participants were registered under Stage 1 and elected to continue their registration under Stage 2.

## New registrations

2.7 The ANAO's previous audit of ACIS found that the department managed new registrations as a self-assessment process. That is, it relied mainly on participants' assertions that eligibility criteria were met, rather than verifying this information. To address this shortcoming, the audit recommended that the department:

... review its registration processes to ensure that they provide adequate assurance that required registration conditions under the *ACIS Administration Act 1999* are met before registration is granted.<sup>32</sup>

2.8 In response to this recommendation, the department developed a procedures manual and a registration checklist in October 2003. The manual

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<sup>29</sup> For example, this includes not having a criminal conviction in the past 10 years.

<sup>30</sup> In assessing applications of national interest, the Minister may have regard to whether the registration would enhance the competitiveness of the Australian automotive industry; provide significant benefits to the Australian economy; introduce significant innovations to the automotive industry; generate significant employment or investment opportunities; or have significant strategic, regional or environmental impacts.

<sup>31</sup> That is, 15 automotive component producers; two automotive machine tool producers; and three automotive service providers.

<sup>32</sup> ANAO, *op. cit.*, pp. 44–47.

sets out the key actions that ACIS staff must take when assessing new applications, and for validating the information supplied. These actions include:

- visiting the applicant's office and manufacturing site to verify the production, sales and investment information supplied, and to assess whether the applicant understands its obligations under the Act; and
- conducting a search on the Australian Securities and Investment Commission (ASIC) website to determine whether the applicant is a registered company, and to assist in assessing whether the applicant meets the 'fit and proper person' test.

2.9 The ANAO examined five of the 20 new registrations for Stage 2 and found that, overall, ACIS staff had undertaken the appropriate actions to validate the applicants' claims, and recorded these on the registration checklist. In two cases a site visit was not undertaken during the registration process. DIISR advised that, where a previously registered company has re-applied for registration, either as part of a group of companies or as a new legal entity, a site visit was not essential because details of the company's operations were already known. In such cases, a site visit may be undertaken in the following 12–18 months, as per DIISR's normal cycle of company visits.

2.10 Also, the five new registrations were finalised within the appropriate timeframe<sup>33</sup>, and the decision to register each applicant was made by the appropriate officer, in accordance with DIISR's instrument of delegation.

### **Assessing ongoing eligibility**

2.11 As the number of new registrations in Stage 2 is low compared to the overall number of participants, DIISR's main focus is ensuring that existing participants meet registration requirements on an annual basis. The department's primary means of assessing participants' ongoing eligibility are:

- monitoring the production and sales figures reported in participants' quarterly claim forms, to identify whether participants are on track to meet the relevant production criterion. For example, MVPs must produce at least 30 000 motor vehicles or engines each year; and
- conducting ASIC checks and obtaining 'intelligence' to track developments in the industry (such as changes in company ownership)

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<sup>33</sup> DIISR is required to assess an application within 60 days, or a longer period if additional information is required to be provided by the applicant.

and to determine whether participants continue to meet the 'fit and proper person' criteria.

2.12 DIISR advised the ANAO that, as of 30 June 2007, ten participants have been deregistered during Stage 2. Of these, eight were deregistered at the participants' request; one company had gone into liquidation; and another had ceased operations.

2.13 The ANAO examined a sample of ten participant files and found that DIISR had monitored whether ongoing registration requirements were being met. The ANAO notes that DIISR does not usually verify the sales and production figures provided in participants' quarterly claims forms. However, the department seeks to manage this risk by confirming these details during any subsequent compliance audit or site visit to a participant's premises.<sup>34</sup> If the participant is found to be ineligible, DIISR can recover any duty credits previously issued.

## Processing participants' claims

2.14 ACIS participants are required to submit a claim form to DIISR within 45 days after the end of each quarter. The claim form, known as a quarterly return, sets out details of expenditure on eligible activities. For example, MVPs provide details on the production of motor vehicles, and any investment in P&E or in R&D.

2.15 DIISR captures the information provided by participants in its Integrated Program Management System (IPMS). IPMS checks to ensure that participants have provided all the required information, including checking whether the return was received within the required timeframe. If the quarterly return is complete, duty credits are calculated automatically within IPMS and issued to participants before any further checking takes place.

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<sup>34</sup> DIISR's arrangements for checking the integrity of participants' claims are discussed in Chapter 3 of this report.

## Calculating duty credits

2.16 The key steps in calculating duty credits in IPMS involve:

- calculating the amount of unmodulated credits to which a participant is entitled, according to the relevant formula provided in the Act;
- applying a modulation rate<sup>35</sup> to the unmodulated credits, to ensure that the funding caps for both MVPs and supply chain participants are not exceeded; and
- reducing the modulated credits, if necessary, to ensure that total credits allocated to each participant do not exceed five per cent of any participant's previous year's sales of ACIS goods and services.

2.17 When duty credits amounts are finalised, they are posted to each participant's account in the ACIS ledger (which sits within IPMS). From there, the credits can be transferred to Customs, to offset the duty on eligible imports, or used for other approved purposes. This includes being traded with other Scheme participants.<sup>36</sup>

### *Integrity of duty credit calculations*

2.18 During the transition from Stage 1 to Stage 2 in early 2006, DIISR made two errors in the calculation of duty credits, which led to the incorrect issuing of credits for some participants. These errors occurred because some of the changes in the funding parameters for Stage 2 were not incorporated into IPMS.<sup>37</sup> In turn, this was largely due to weaknesses in DIISR's application development practices. DIISR has since rectified these errors, and improved its processes for updating and releasing applications.

2.19 The ANAO examined DIISR's current processes and controls for calculating duty credits and found that:

- appropriate controls have been implemented within IPMS to preserve the completeness, accuracy and reliability of Stage 2 data;
- appropriate IT procedures and controls are in place to ensure the eligibility of Stage 2 participants applying for duty credits;

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<sup>35</sup> A simple explanation of modulation is provided in paragraph 2.21.

<sup>36</sup> The transfer and use of duty credits is discussed further in Chapter 4 of this report.

<sup>37</sup> One of these errors was the incorrect application of the modulation rate for MVP investment credits for the first three quarters of Stage 2. This error resulted in DIISR underpaying around \$1.5 million in duty credits for quarters one, two and three of 2006.



- the algorithms set up in IPMS to calculate duty credits correspond to the formulas in the Act—that is, the system enables credits to be calculated accurately; and
- appropriate controls are in place to ensure that duty credits are allocated within the five per cent sales cap.

### *Timeliness of duty credit payments*

2.20 DIISR has set an internal target of 10 calendar days to process participants' quarterly returns. The ANAO examined duty credit payments for the first five quarters of Stage 2 and found that 75 per cent of claims (some 861) were paid within the timeframe. Claims that were not processed within the timeframe included 290 quarterly returns, which were delayed because of an Administrative Appeals Tribunal decision.<sup>38</sup> In brief, the Tribunal found that the Act provided the department with limited grounds to recover credits once those credits had been allocated. As a consequence, the department took the prudent approach of delaying the issuing of credits until it had the power to recover any incorrectly claimed amounts.<sup>39</sup>

## Managing the modulation process

2.21 DIISR's key mechanism for adhering to the \$2 billion funding cap for Stage 2 (as with Stage 1) is by setting a modulation rate to reduce participants' claims, where those claims are forecast to exceed the available credits. For example, if the modulation rate is set at 0.80, participants receive the equivalent of 80 cents for every duty credit they are eligible to receive. The *ACIS Administration (Modulation) Guidelines 2006* detail DIISR's processes for determining the modulation rates for Stage 2.

### Modulation for Stage 2

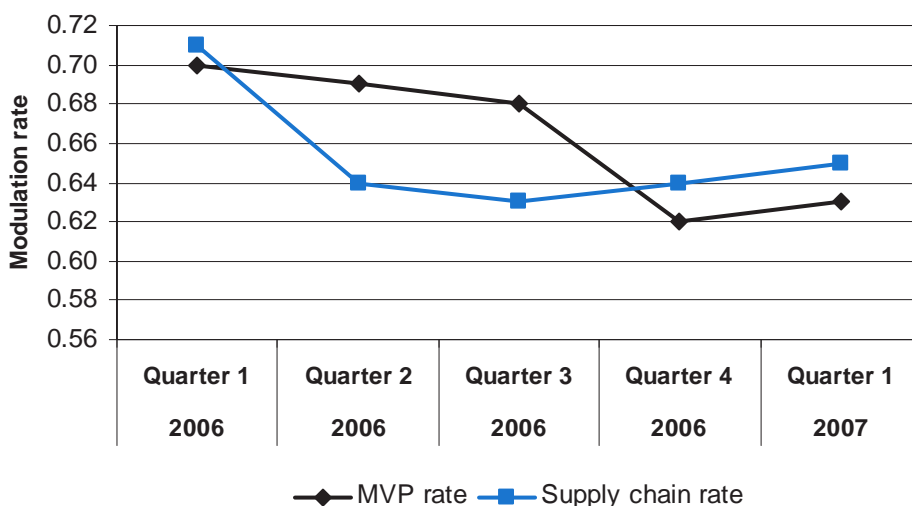
2.22 In Stage 2 (and Stage 1) the demand for credits has exceeded the credits available from the \$2 billion capped funding pool. Since the start of Stage 2, the modulation rate has fluctuated between 0.70 and 0.62 for MVPs, and between 0.71 and 0.63 for supply chain companies. These rates are shown in Figure 2.1.

<sup>38</sup> Spicer Axle Structural Components Australia Pty Ltd and Secretary, Department of Industry, Tourism and Resources [2006] AATA 1004 (24 November 2006).

<sup>39</sup> This power was obtained through an amendment to the *ACIS Administration Act 1999* on 15 March 2007, and, as an interim measure, by requesting participants to sign a Deed of Undertaking to enable the department to recover any duty credits found to be inappropriately claimed.

**Figure 2.1**

**Modulation rates for ACIS Stage 2, Quarter 1 2006 to Quarter 1 2007**



Source: ANAO analysis of Department of Innovation, Industry, Science and Research' data

2.23 DIISR advised the ANAO that in 2007–08 it proposes to engage an external party to independently review its modulation model, as it had done in 2003 for the modulation model used for Stage 1.

**Modulation for Stage 1**

2.24 In Stage 1, DIISR allocated all but \$1 million in duty credits from the \$2 billion cap, which represents some 99 per cent of all available credits. DIISR was able to allocate nearly all credits through an additional allocation of credits at the end of Stage 1. This allocation was calculated and distributed through a second modulation of final quarter claims. The final allocation was made in November 2006, allowing DIISR to resolve outstanding compliance activities and recover any mis-claimed credits. These credits were then able to be reallocated to Scheme participants.

2.25 While there was some delay in the final allocation of credits, the ANAO considers that, on balance, DIISR's process for allocating remaining credits was appropriate to ensure that the maximum number of credits could be allocated and the funding cap maintained.

## Administration of the MVP R&D Scheme

2.26 Under the \$150 million MVP R&D Scheme, the four Australian MVPs (Ford, Holden, Mitsubishi and Toyota) were invited to submit proposals for R&D projects to the Industry Research and Development (IR&D) Board. Projects were assessed and ranked against the following four merit criteria:

- calibre of new R&D activity that will be generated in Australia;
- technical merit of the project;
- level of benefit, including environmental benefit to the wider Australian community; and
- contribution of the project to the sustainability of an internationally competitive automotive industry in Australia.

2.27 Of the available \$150 million in duty credits, \$142.9 million has been allocated to the MVPs to undertake 12 R&D projects that were approved through two funding rounds. A breakdown of the duty credits allocated is provided in Table 2.2.

**Table 2.2**

### Duty credits allocated under the MVP R&D Scheme

MVP	Round 1	Round 2	Total
Ford	\$27 980 000	\$47 020 000	\$75 000 000
Holden	\$7 820 000	\$48 300 000	\$56 120 000
Mitsubishi	n/a	\$1 100 000	\$1 100 000
Toyota	\$5 560 000	\$5 150 000	\$10 710 000
<b>Total</b>	<b>\$41 360 000</b>	<b>\$101 570 000</b>	<b>\$142 930 000</b>

Source: ANAO analysis of the Department of Innovation, Industry, Science and Research's data

2.28 The balance of the funds not allocated under the MVP R&D Scheme has been returned to the MVPs component of the capped funding pool<sup>40</sup> under a separate initiative called the Supplier Capability Development Program. Through this program, MVPs can receive funds to undertake projects that enhance the capabilities of Australian automotive components suppliers, and enable them to identify and secure emerging opportunities in international supply chains.

<sup>40</sup> That is, 55 per cent of the \$2 billion capped pool.

## Management of claims

2.29 DIISR has signed a funding agreement with each MVP, which sets out the general conditions of the MVP R&D Scheme and the particular conditions for each approved project. To claim credits, MVPs are required to provide details of expenditure and progress against milestones in a quarterly return. Claims are then processed under DIISR's normal procedures, although these credits are not subject to modulation.

2.30 At 30 June 2007, DIISR had paid a total of \$18.7 million in duty credits under the MVP R&D Scheme.

### *Monitoring project expenditure and milestones*

2.31 DIISR monitors compliance with the conditions and milestones of the funding agreements by:

- reviewing the quarterly returns provided by MVPs, to identify any issues with the integrity of the claim; and
- visiting the MVPs' premises to discuss and review the status of projects.

2.32 The ANAO examined a sample of participant files for the MVP R&D Scheme and found that DIISR is monitoring participants' claims, and is taking appropriate steps to ensure that payments are made only when participants have met the conditions stated in their funding agreement. For example, in one case, DIISR found that an MVP had overstated its base R&D expenditure by \$100 million, potentially meaning that the MVP would not be eligible for some of their allocated project funds. During this audit, DIISR was examining the potential overstatement and considering its options for providing ongoing assistance to this MVP. In the meantime, it had determined that no further credits would be provided until the issue has been resolved.

2.33 One of DIISR's key requirements in monitoring projects is identifying whether the MVPs actual expenditure on a funded project in one year is less than 75 per cent of forecast expenditure for that project. Where this occurs, credits allocated (but not yet issued) to the MVP for projects for future years must be returned to the Scheme, unless DIISR approves a variation to that expenditure.

2.34 DIISR advised the ANAO that of the 12 approved projects four have been varied. There are another seven projects currently under consideration for variation by DIISR. These variations mean that projects are not meeting their

original timetable, as submitted to the IR&D Board. This creates a risk that projects may not be completed by the end of Stage 2, which, ultimately, may impact on the intended outcomes for the MVP R&D Scheme. As such, this aspect of the Scheme requires ongoing and close monitoring by DIISR and the IR&D Board.

## Conclusion

2.35 DIISR has established an effective control framework to comply with legislative requirements and to manage the financial risks relating to the issuing of duty credits. The department has well-developed processes to assess the eligibility of participants to receive credits; to calculate individual duty credits claims accurately, based on the information provided by participants; and to adhere to the funding limits for the Scheme.

2.36 The department has also implemented appropriate processes to manage the allocation of credits under the \$150 million MVP R&D Scheme. This includes monitoring whether participants are complying with the requirements of their funding agreements, and taking appropriate actions when these requirements have not been met.

## 3. Claims made by Scheme Participants

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*This chapter examines DIISR's arrangements for promoting accurate claiming by ACIS participants, and for checking the integrity of participants' claims.*

### Introduction

3.1 As previously noted, DIISR administers ACIS on a 'self-assessment' basis. That is, participants determine what they are entitled to claim under the Scheme, and the department issues duty credits based on their quarterly claims. This approach allows duty credits to be provided on a timely basis. It also means that DIISR needs to manage the risk of mis-claiming, to ensure that duty credits are issued appropriately and equitably.

3.2 The ANAO examined DIISR's arrangements for assisting participants to lodge accurate claims, and for checking the integrity of participants' claims.

### Promoting accurate claiming

3.3 The Act and Regulations prescribe the type of activities and expenditure that participants can claim for under ACIS. The department promotes awareness of these requirements by:

- publishing information on AusIndustry's website, including eight customer guidelines on topics such as *Completing Application for Registration Forms* and *Completing Quarterly Return Forms*;
- assigning a customer service manager (CSM) to each participant, to serve as the focal point for participants' queries about the Scheme;
- producing an ACIS newsletter periodically and holding occasional industry forums to discuss issues about the Scheme; and
- maintaining contact with the peak bodies that represent Australian motor vehicle producers and automotive component manufacturers.<sup>41</sup>

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<sup>41</sup> The Federal Chamber of Automotive Industries is the peak body for the motor vehicle industry, while the Federation of Automotive Products Manufacturers represents automotive component producers.

3.4 DIISR's customer guidelines are relatively current (re-issued in November 2006<sup>42</sup>) and provide clear, step-by-step instructions to assist participants to provide the information required by DIISR. Three customer guidelines also include specific guidance on the type of documentation that DIISR requires participants to have available to substantiate their claims.<sup>43</sup> The 'substantiation guidelines' are aimed at assisting the process of self-assessment, and are intended to represent the minimum records required to comply with the Act.

### **Feedback by Scheme participants**

3.5 ACIS participants who provided feedback to the ANAO during the audit acknowledged that DIISR has a range measures to promote accurate claiming. However, their key message was that DIISR should be more proactive in providing advice on the type of activities that can be legitimately claimed for under the Scheme, rather than relying on compliance audits—which take place after duty credits have been issued—to examine participants' understanding and application of the rules.

3.6 Some participants suggested that more regular industry briefings should be held to clarify DIISR's position in relation to claims that may be open to interpretation, for example some offshore R&D claims. The last industry briefing was held in December 2003. Other participants suggested that DIISR could improve the range and specificity of its guidance material, to focus on those areas where mis-claiming had been found.

3.7 While recognising that DIISR has a range of useful measures in place to educate participants on Scheme requirements, the ANAO agrees that there are opportunities for the department to do more in this area. In particular, the level of mis-claiming identified through the department's compliance activities (as discussed in paragraphs 3.9 to 3.13) suggests that additional and more targeted guidance could improve the level of voluntary compliance.<sup>44</sup> Such measures are likely to be more cost-effective than increasing the level of compliance activities following the issuing of duty credits.

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<sup>42</sup> One exception was the *Guide to Claiming Contracted R&D*, which was last issued in October 2001. However, the guideline was under review at the time of this audit.

<sup>43</sup> These are: the *Guide to Completing Application for Registration Form*; the *Guide to Completing Business Plans*; and the *Guide to Completing Quarterly Return Forms*.

<sup>44</sup> The ANAO recognises, however, that some mis-claiming may be deliberate and therefore does not necessarily reflect any shortcomings in DIISR's efforts to promote accurate claiming.

## Identifying mis-claiming

3.8 Since ACIS began on 1 January 2001, DIISR has identified some \$141 million in ineligible activities claimed by participants, as of 30 June 2007. This has resulted in \$21.5 million in credits being returned to the main funding pool, and being made available to other participants.

3.9 DIISR identifies mis-claiming by conducting compliance audits on selected participants, and by using CSMs to review participants' quarterly claim forms. CSMs may also verify some aspects of participants' claims during site visits to participants' premises. For example, confirming that capital equipment previously claimed exists, and is allowable under the Regulations.

### Compliance role of customer service managers

3.10 The ANAO examined a sample of claim files and found that CSMs are reviewing participants' quarterly claims forms on a timely basis. They also maintain regular contact with participants through phone calls, correspondence and site visits. Data provided by DIISR indicates that CSMs identified around \$6.7 million in incorrectly claimed duty credits during the period 1 January 2004 to 28 February 2007—some 38 per cent of all debts identified in this period.

3.11 Although CSMs play an important role in administering ACIS, their capacity to detect mis-claiming is limited by the following three factors:

- the primary role of CSMs, as noted in DIISR's internal guidance material, is to establish a strong business relationship with participants, and to encourage voluntary compliance with the Scheme. It is not to conduct a forensic examination of participants' claims, as happens during a compliance audit;
- CSMs are not presently required, nor sufficiently resourced, to conduct an annual site visits for all participants. In 2006–07, a target of 140 site visits was set, which represents 58 per cent of all participants. Moreover, because most site visits take less than one day, CSMs do not have time to examine claims in detail; and
- although some CSMs conducted compliance audits in Stage 1, not all current CSMs possess the relevant skills, qualifications or experience to undertake detailed reviews to the standard required by a compliance audit, and in accordance with professional auditing standards.



3.12 These limitations mean that, in practice, compliance audits are DIISR's best tool for identifying mis-claiming.

## Compliance audits

3.13 Compliance audits are undertaken at participants' premises and involve an examination of one or two claim forms from previous quarters. Their purpose is to determine whether the production and / or investment details in the claim forms can be substantiated, and to identify any duty credits that participants were not entitled to receive.

### Conduct and methodology of compliance audits

3.14 The ANAO's previous audit of ACIS found that there were limitations in the guidance given to ACIS staff on conducting audits, and variable quality in the management of audits. This included a lack of substantive testing and properly conducted statistical samples.<sup>45</sup> Since this audit, DIISR has enhanced its approach to conducting compliance audits. In July 2003, it issued a *Risk and Audit Handbook* for ACIS staff, which provides procedures and guidance on conducting compliance audits, including on audit planning and audit sampling. The ANAO examined a sample of completed audit files and found that the standard of documentation was consistently high and conformed to the *Handbook*. Also, there was evidence of management review on all files, which served to improve the rigour and consistency of audit findings.

3.15 Another key change since the ANAO's previous audit is that ACIS compliance audits are now undertaken by a small team of suitably qualified staff, rather than by CSMs who also have a service delivery role. The audit team works separately to CSMs to avoid any role conflict. However, there is regular interaction between the two groups to share information and to identify and manage compliance risks to the Scheme.

### Selection, coverage and frequency of compliance audits

3.16 DIISR adopts a risk-based approach to examining claim compliance, and uses a risk rating system for selecting participants for audit. Each participant is rated as high, medium or low risk, as determined through 11 risk

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<sup>45</sup> ANAO, op. cit., pp. 69–75.

factors.<sup>46</sup> Participants rated as high and medium risk are given priority for audit over participants rated as low risk.

3.17 Since ACIS commenced in 2001, DIISR has undertaken 184 compliance audits—166 audits in Stage 1 and 18 in Stage 2 as at 30 June 2007. The ANAO examined DIISR's audit data for the 245 participants registered under Stage 2 (as at 31 May 2007) and found that:

- 161 participants, or nearly two thirds, have been audited. Of the 84 participants yet to be audited, 66 also received credits in Stage 1;
- all participants rated as high risk have been audited, as well as 16 (of 17) participants rated as medium risk. This includes the four MVPs and six ACPs, who have collectively received around 75 per cent of all duty credits issued since ACIS began;
- five participants have been audited twice since ACIS began in 2001. This includes one MVP, three ACPs and one AMTP. DIISR is currently conducting its second audit on another MVP; and
- the number of compliance audits completed each year has declined over the past five years, from a high of 37 audits in 2002–03 to 18 in 2006–07. DIISR has set of target of completing 18 audits in 2007–08.

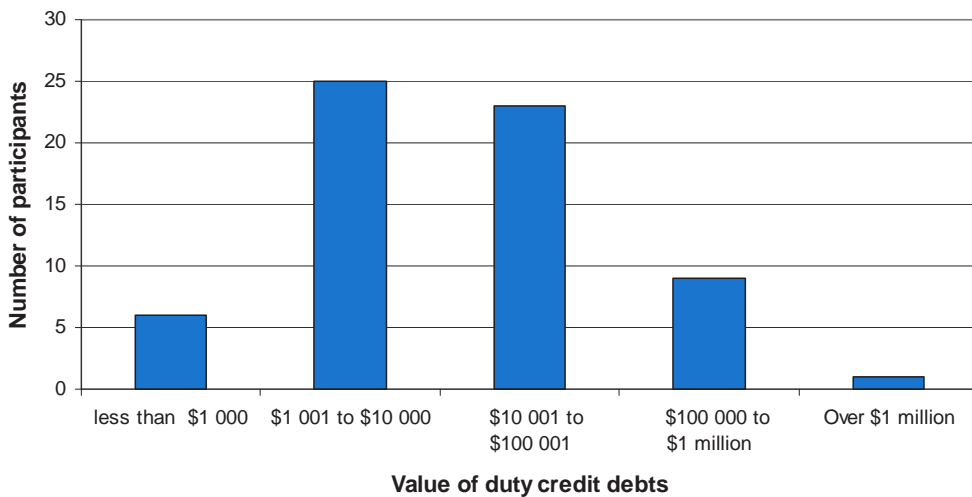
3.18 Overall, DIISR has directed compliance audits at participants rated as high and medium risk, who receive the vast majority of duty credits. However, most participants have been audited only once in the six years since ACIS began.

## **Results of compliance audits**

3.19 The ANAO examined the results of compliance audits undertaken between 2004 and 2007. In 58 of the 84 audits completed during this period (or nearly 70 per cent of audits), DIISR raised a debt to recover duty credits found to be inappropriately claimed. The debts ranged from \$250 to over \$8 million (in one case). However, as illustrated in Figure 3.1, the majority of debts fell within the range of \$1 000 to \$10 000 and then between \$10 000 and \$100 000.

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<sup>46</sup> These factors include eight quantifiable risks, such as the number of duty credits received and any amounts found to have been previously mis-claimed; and three qualitative risks, such as participants' knowledge of the Scheme, as judged by CSMs during site visits.

**Figure 3.1****Duty credit debts identified through compliance audits, 2004 to 2007**

Source: ANAO analysis of Department of Innovation, Industry, Science and Research' data

3.20 Participants found to have claimed duty credits inappropriately are required to repay the credits, either by offsetting the debt against other credits earned, or by repaying the debt through the department's debt management process. The Act allows DIISR to impose a late payment penalty on participants; however no other penalties for mis-claiming apply.

3.21 DIISR takes action to resolve mis-claiming in individual cases by recovering debts and following up on whether 'management actions' listed in compliance audit reports are implemented by participants. These actions are aimed at improving participants' ability to meet Scheme requirements and to submit accurate claims. As well, DIISR has identified some key risks to the Scheme from mis-claiming. For example, the department's 2006–07 compliance management strategy for ACIS identifies vendor tooling and off-shore R&D as major risks to the integrity of participants' claims.

3.22 However, DIISR has not analysed the results of audits on a systematic basis to better target audits and to inform its approach to other compliance activities. For example, DIISR did not maintain management information on the most common types of mis-claiming identified through audits; nor did it maintain aggregate information on the extent of non-compliance in the key areas of the Scheme where claims are made, such as P&E and R&D.

### *ANAO analysis of compliance audits*

3.23 The ANAO analysed the findings of 20 recent compliance audits. In these audits, only two participants were found not to have mis-claimed. DIISR identified 52 occurrences of incorrect claiming, including:

- seven cases where participants were claiming for ineligible P&E items. These items included forklifts, ladders and property improvements that were not directly related to the production of automotive products;
- six cases where participants were claiming R&D that was not directly related to the R&D projects but was ancillary to the process. This included claims for administration costs to report on R&D activities and expenditure on security services;
- nine cases where participants were unable to substantiate their R&D claims (or parts thereof). That is, there was no documentation or explanation to support the claims; and
- five cases where participants incorrectly classified contracted and offshore R&D as direct investment in R&D.

3.24 The analysis of these audit findings indicates that DIISR could develop additional and more targeted guidance material to improve participants' understanding of Scheme requirements, and the level of voluntary compliance. One option could be to post the key findings of audits on DIISR's website on a periodic basis, making this information readily available to participants. Another option is to provide this information through other established communication channels such as the ACIS newsletter or a direct mail-out to participants.

### *Targeting and scope of compliance audits*

3.25 As well as using the results of compliance audits to better educate and inform participants, DIISR should use this information to target specific types of mis-claiming. For example, if the analysis of audit findings indicates a higher level of mis-claiming in certain R&D activities, compliance audits could focus on this specific issue, rather than attempting to examine all aspects of a claim, as currently happens. Audits with a stronger focus on high risk areas are likely to be more cost-effective, providing capacity to increase the extent of coverage.

3.26 The analysis of audit findings could also assist in targeting specific participants that pose a higher risk of mis-claiming in certain areas. For

example, if analysis identified that a particular supply chain sector was disproportionately represented in duty credits debts, DIISR could target its audits on this sector. There may also be merit in publicising DIISR's compliance strategy for ACIS. This approach has been used successfully by other agencies including the Australian Taxation Office and Customs, and can have an educative as well as a deterrent effect.

## Conclusion

3.27 DIISR has established the key components of a compliance framework to promote accurate claiming and to identify any mis-claiming by Scheme participants. In particular, DIISR has directed compliance audits at participants rated as high and medium risk, who receive the significant majority of duty credits. However, the relative infrequency of audits, coupled with limitations in the compliance role played by CSMs, means that DIISR relies, to a large degree, on the voluntary compliance of participants.

3.28 While DIISR uses various methods to assist participants to lodge accurate claims, the level of mis-claiming identified to date suggests that further efforts are needed in this area. In particular, there is an opportunity for DIISR to systematically analyse, and use, the findings from its compliance activities to improve participants' understanding of Scheme requirements, and to better inform its approach to determining the coverage and scope of compliance audits.

## Recommendation No.1

3.29 The ANAO recommends that the Department of Innovation, Industry, Science and Research systematically analyse and use the results of compliance activities of the Automotive Competitiveness and Investment Scheme to:

- (a) inform its approach to promoting accurate claiming by Scheme participants; and
- (b) determine the coverage and scope of future compliance audits.

## DIISR's response

3.30 Agreed. The department's compliance activities covering scheme participants are based on a sound risk management approach. All participants are actively monitored at the quarterly return stage and the department conducts detailed audits of scheme participants rated medium and high risk. To date all high risk participants and all but one medium risk participant have

been audited. While the department takes into account audit outcomes in risk rating scheme participants and in targeting its audits, it sees merit in placing the analysis of compliance outcomes on a more systematic basis. Design of a formal, systematic approach to analysing audit outcomes was underway before the ANAO audit commenced and is expected to be completed soon.

## 4. Use of ACIS Duty Credits

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*This chapter examines whether duty credits transferred to Customs are used only on eligible imports, and are properly accounted for by DIISR.*

### Introduction

4.1 Once duty credits have been issued to Scheme participants, they can be:

- traded among participants;
- used to repay an ACIS debt;
- applied to offset the duty payable on eligible imports<sup>47</sup>; or
- applied against an earlier payment of duty on eligible imports, to obtain a refund.

4.2 DIISR facilitates the trading of credits among participants, manages the repayment of credits against ACIS debts, and transfers duty credits to Customs. In turn, Customs manages the application of duty credits to eligible imports, and provides refunds to participants for duty previously paid.

4.3 The ANAO examined whether duty credits transferred to Customs are used only on eligible imports, and are properly accounted for by DIISR.

### ACIS ledger

4.4 As required by the Act, DIISR has established a ledger to record the number of duty credits held by Scheme participants. The ledger is maintained within IPMS and has been divided into three parts, one for each ACIS stage. The ledger for Stage 2 covers transactions from 1 January 2006 to 31 December 2011.

4.5 Within the ledger, an account is created for each participant, which operates in a similar manner to a bank account whereby credits can be transferred in and out. When participants first register in the Scheme, they are given an ACIS customer number, which identifies their ledger account, and a password to access their account in IPMS. A new number and password was provided to each participant at the start of Stage 2. Participants can view (but not edit) the ledger; obtain information on credits issued; apply to transfer

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<sup>47</sup> Certain motor vehicles and related parts.

or sell credits to another party; verify past transactions; and find out their duty credit balance.

## **Trading of duty credits among participants**

4.6 The trading of duty credits allows participants who do not import eligible goods to obtain a financial benefit from ACIS by selling their duty credits to other participants, or to third-parties, known as 'ledger participants'. Ledger participants are not registered under ACIS and do not earn credits. However, they can purchase credits from registered participants and use those credits as they see fit. For example, companies that import vehicles into Australia may purchase credits to offset the duty on those vehicles. Duty credits can be purchased for less than their nominal value of one Australian dollar, providing savings to the importers.

4.7 At 30 June 2007, there were 245 registered participants in Stage 2 and 30 ledger participants. Of these, 27 registered participants and 16 ledger participants were actively transferring credits to Customs. The remaining participants chose to trade their credits with other ACIS participants and had not transferred their credits to Customs.

4.8 Once traded, duty credits must ultimately be used to offset the duty payable on eligible imports, otherwise they expire at the end of each ACIS stage.<sup>48</sup>

## **Transfer and use of duty credits at Customs**

4.9 Participants who wish to transfer duty credits to Customs must obtain an Import Credit Number (ICN) from DIISR. An ICN functions like an account at Customs, to which credits can be transferred and then used. By the end of Stage 1, more than \$2.8 billion in duty credits had been transferred from DIISR to Customs, with a further \$608 million transferred in Stage 2, to 30 June 2007.

4.10 The key steps in the transfer process are summarised below:

- ACIS participants (registered participants or ledger participants) request DIISR to transfer credits to Customs;
- DIISR extracts the requested number of credits from the participant's ledger account, and sends a batch record to Customs by secure email (usually several times per week);

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<sup>48</sup> For example, the duty credits issued in Stage 2 are set to expire on 31 December 2011.



- Customs manually keys the transaction details into the Tariff Concession System (TARCON), and provides confirmation to DIISR that the correct amounts have been recorded as per the batch record; and
- Customs electronically transfers the ACIS data from TARCON to the Integrated Cargo System (ICS), allowing ACIS participants to use the credits on eligible imports.

4.11 The current transfer arrangements have reduced the level of manual handling of data found during the ANAO's previous audit of ACIS.<sup>49</sup> However, this process continues to involve a degree of manual processing, which increases the risk of error. In turn, this risk requires additional controls to be implemented by both agencies, especially Customs.

4.12 Both agencies have recognised the limitations of the current arrangements and are re-trialling a fully automated transfer process. This process, which is expected to be in place in early 2008, involves duty credit data being sent directly from DIISR to Customs' ICS, removing the need for Customs' staff to manually key data into TARCON.

### **Application of duty credits to eligible imports**

4.13 The *Customs Tariff Act 1995* prescribes the eligible imports to which participants can apply ACIS duty credits. These include certain motor vehicles for the transportation of passengers and goods, including used and second-hand vehicles, and certain components for those vehicles.<sup>50</sup>

4.14 The use of ACIS credits for eligible imports is managed within ICS. In brief, this involves importers or customs brokers accessing their account in ICS; completing an import declaration, which lists the items to be brought into Australia; and then paying the duty on those items. Some examples of eligible goods that duty credits are applied against are listed in Table 4.1.

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<sup>49</sup> See ANAO, *op. cit.*, pp. 56–57.

<sup>50</sup> See Chapter 87 of Schedule Three of the Customs Tariff Act which lists the relevant tariff classifications for ACIS, namely: 8702, 8703 and 8704.

**Table 4.1****Top 10 imported items for which ACIS duty credits were used to offset customs duty, July to September 2007**

Imported item	Number of units
1. New passenger motor vehicles (cylinder capacity between 1500 and 3000 cc)	9887
2. New diesel passenger motor vehicles (cylinder capacity between 1500 and 2500 cc)	5238
3. Other passenger motor vehicle parts (not being bumpers, body parts, brakes, gear boxes, drive-axles, wheels or suspension systems)	1986
4. Other diesel motor vehicles for the transport of goods (not exceeding five tonne)	1612
5. Other motor vehicles for the transport of persons (cylinder capacity between 1500 and 3000 cc)	1566
6. Passenger motor vehicle body parts and accessories, not including bumpers	1463
7. Other diesel motor vehicles for the transport of persons (cylinder capacity exceeding 2500 cc)	1255
8. Other screws and bolts	1225
9. Petrol or diesel engine parts, other than for aircraft engines	1188
10. New passenger motor vehicles (cylinder capacity exceeding 3000 cc)	1010

Source: Australian Customs Service

4.15 The ANAO found that Customs has a sound framework to manage the use of ACIS credits for eligible imports. Application controls within ICS restrict the use of credits to items that appear in a 'drop down' list in ICS. In turn, these items correspond to the eligible items prescribed under the Customs Tariff Act. The ANAO examined a sample of transactions and did not identify any instances of duty credits being used on ineligible items. Further, end-dating of ICNs within ICS prevents credits from being used outside the timeframes for each ACIS stage.

4.16 The broader risk that items imported into Australia may not match the items listed on import declarations is addressed through Customs' risk profiling and compliance management strategies. While Customs does not have specific measures to monitor the use of ACIS credits on eligible imports, it does have various strategies to monitor the importation of motor vehicles

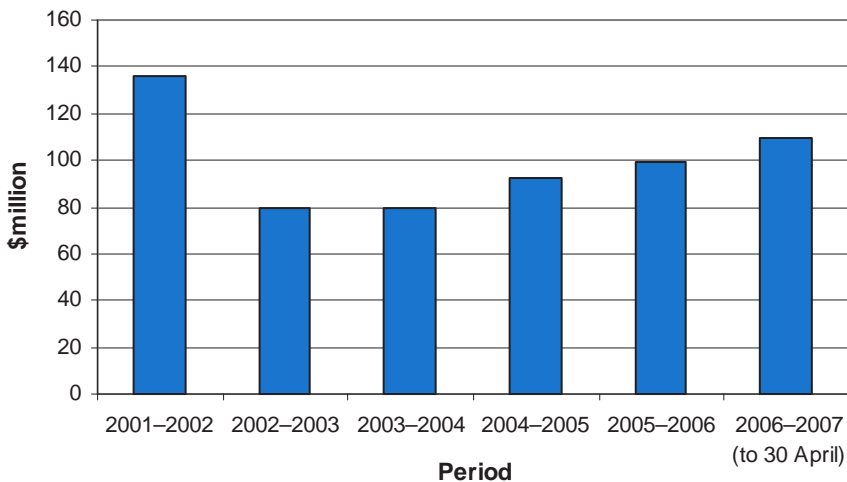
generally, as they provide a significant percentage of annual duty revenue.<sup>51</sup> These measures include establishing profiles to identify high-risk imports and conducting post-transaction audits on certain consignments.

## Refund of duty paid

4.17 To request a refund of customs duty previously paid, ACIS participants are required to lodge a refund claim form with Customs, either by post or electronically. Since 2001, Customs has refunded nearly \$600 million of customs duty to participants. Annual aggregate amounts range from around \$80 million to more than \$136 million, as illustrated in Figure 4.1.<sup>52</sup>

**Figure 4.1**

### Refunds provided to ACIS participants, for the period 2001–02 to 2006–07



Source: ANAO analysis of Australian Customs Service data

4.18 As part of the 2006–07 financial statement audit, the ANAO examined Customs' controls over the payment of refunds generally (not just for ACIS), and assessed the controls to be satisfactory. These controls include sign-off by two officers before refunds are paid; documented procedures on the refund process; and profiles and alerts for certain refund activities. For example, for ACIS, a profile has been established in ICS to identify refunds over a particular

<sup>51</sup> For example, in 2005–06, duty on passenger motor vehicles, excluding the use of ACIS duty credits, accounted for some 11 per cent (or \$538 million) of all duty collected.

<sup>52</sup> Regulation 126 of the *Customs Regulations 1926* sets out Customs' powers for providing refunds to ACIS participants (and for other purposes).

dollar threshold. These refunds are subject to additional scrutiny before payment is approved.

4.19 The ANAO also examined a sample of seven refunds provided to ACIS participants and found that the correct refund was provided in exchange for the correct number of ACIS duty credits. Further, all refunds related to initial transactions that occurred on or after 1 January 2001, as required by the Act.

## Accounting for the use of duty credits

4.20 The requirement for DIISR to maintain records on duty credits held by participants includes those credits transferred to, and used, at Customs.<sup>53</sup> In addressing this requirement, DIISR has implemented a reconciliation process with Customs, which is designed to:

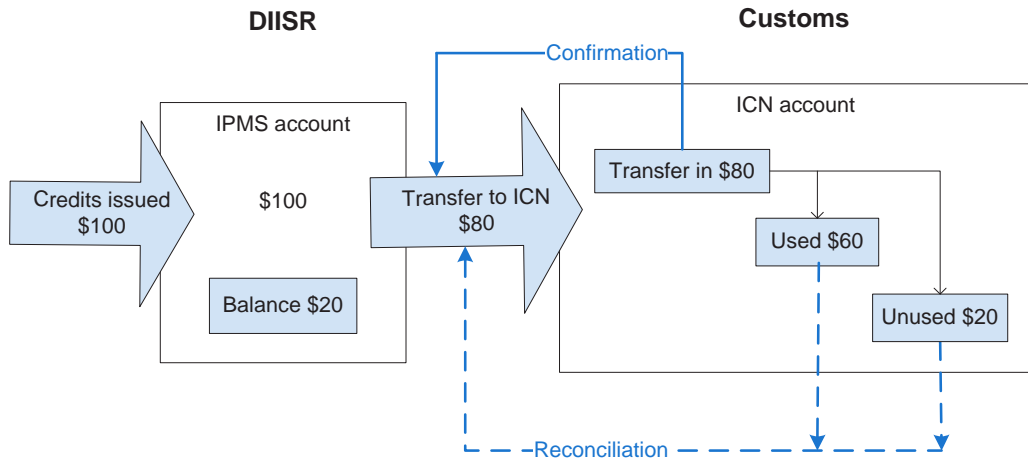
- identify any discrepancies in the agencies' records, which might indicate an error in the initial transfer of credits, or an error in participants' ICN accounts, relating to the use of credits; and
- validate the balance of unused credits at Customs, which represent a liability to DIISR<sup>54</sup>, to be reported in its financial statements.

4.21 Since January 2007 reconciliations have been performed on a monthly basis. Also, in 2006 DIISR conducted a 'whole-of-life' reconciliation covering all of Stage 1 and the first 12 months of Stage 2, to 31 December 2006. A simplified example of the reconciliation process is depicted in Figure 4.2, while the accounting treatment for duty credits is outlined in Appendix 3.

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<sup>53</sup> See section 66 of the *ACIS Administration Act 1999*.

<sup>54</sup> The ACIS liability is made up of the balance of unused duty credits at Customs, the balance of credits in participants' accounts at DIISR, and any accrued credits.

**Figure 4.2****Reconciliation of duty credit transfers between DIISR and Customs**

Source: ANAO

**Outcome of reconciliation and reporting processes**

4.22 DIISR and Customs have identified some significant discrepancies or errors between their records. In particular, at 30 June 2006, there was a variance of around \$136 million between the expected balance of unused duty credits at Customs, and the actual balance reported by Customs. Of this amount, some \$122 million was subsequently found to relate to an inaccurate balance provided by Customs for one Scheme participant. Also, in 2006 a Scheme participant was credited with nearly \$12 million more in duty credits by Customs than had been transferred by DIISR.

4.23 Customs advised the ANAO that, while some risk to revenue may have resulted from these discrepancies, it actively monitored related import transactions in consultation with affected ACIS clients, and with DIISR. In addition, Customs advised that it completed a full reconciliation of all client records by early July 2006 to ensure that the balance of import duty credits in each client's account was appropriate and properly accounted for.

4.24 DIISR and Customs have since resolved the majority of the discrepancies between their records, and have rectified the \$12 million overpayment. However, the ANAO identified some weaknesses in the agencies' governance arrangements and day-to-day procedures for managing the transfer of duty credits, which have increased the risk of errors occurring:

- although ACIS has been running since 2001, DIISR and Customs have yet to document agreed policies and procedures addressing their roles and responsibilities for managing the transfer, use and reporting of duty credits;
- prior to June 2006, reconciliations were performed infrequently, limiting DIISR's ability to identify errors in the transfer of credits and to report accurately on the balance of unused credits at Customs; and
- officers from both agencies did not have a complete understanding of the current reconciliation process<sup>55</sup>, limiting their ability to identify and correct errors in the reconciliation reports produced since June 2006.

4.25 To address these weaknesses, a more comprehensive and regular reconciliation process is being put in place between the agencies. For example, DIISR has implemented a formal sign-off process for each monthly reconciliation report. Also, in August 2007 a workshop was held between the agencies to obtain a more informed understanding of the reconciliation process. The monthly reconciliations performed in 2007 have identified immaterial variances between the agencies' records.

## **Financial statement issues**

4.26 The ACIS duty credit liability is a significant Administered balance sheet item in DIISR's financial statements. It comprises the balance of unused duty credits recorded by Customs, the balance of credits in participants' accounts recorded by DIISR, and any accrued credits. During its audit of DIISR's 2006–07 financial statements, the ANAO found that:

- the ACIS liability reported within the draft financial statements was overstated by more than \$150 million (although this overstatement was subsequently corrected in the final statements); and
- there was an unreversed accrual from 2001 amounting to \$146 million that had not been updated to reflect the estimate of credits issued in relation to the final quarter of 2006–07.

4.27 The ANAO also found that DIISR's internal procedures did not include a complete reconciliation of ACIS data from the program area (based in Melbourne) with the data subsequently entered into its financial management system, and reported externally. The absence of a full reconciliation increased

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<sup>55</sup> For example, officers were initially unable to tell the ANAO where all the data used to perform the reconciliation was sourced from within the other agency.

the risk that the ACIS liability could be mis-reported, potentially resulting in a material error in DIISR's financial statements.

## Conclusion

4.28 DIISR and Customs currently have workable arrangements to manage the transfer of duty credits in a timely and secure manner. The agencies are presently trialling a more automated approach to reduce the level of manual intervention in the credit transfer process. Testing undertaken by the ANAO indicates that duty credits transferred from DIISR to Customs are being applied appropriately to eligible imports, or to obtain a refund of duty previously paid.

4.29 However, DIISR's processes to account for transferred duty credits have not been sufficiently robust in recent years. This has affected the department's ability to identify errors in participants' duty credit accounts, and to report accurately on ACIS, including in its financial statements.

4.30 Although a more comprehensive reconciliation process is being put in place between DIISR and Customs, the agencies have yet to document procedures, and strengthen their governance arrangements, to better manage the risks surrounding the transfer, use and reporting of duty credits.

## Recommendation No.2

4.31 The ANAO recommends that the Department of Innovation, Industry, Science and Research and the Australian Customs Service review their governance arrangements, and document procedures, to support their respective responsibilities for managing the transfer, use and reporting of duty credits under the Automotive Competitiveness and Investment Scheme.

### DIISR's response

4.32 Agreed. The department notes the ANAO's finding that Customs and the department have workable arrangements in place to manage and transfer credits in a timely and secure manner. The department agrees that documentation and processes around reconciling the ACIS records of the two agencies can be improved. It is expected that this will be in place early in the new calendar year.

## **Customs' response**

4.33 Agreed. Customs recognises the need to update and further develop procedural documentation with DIISR to ensure that the responsibilities of each agency are more clearly defined. The current documents and processes between Customs and DIISR are being revised and are expected to be finalised in early 2008.



## 5. Effectiveness of the Scheme

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*This chapter examines how DIISR measures and reports on the effectiveness of ACIS in meeting intended program outcomes.*

### Introduction

5.1 ACIS is the Australian Government's key measure for supporting the automotive industry, which is legislated to run until 2015. As previously noted, the purpose of the Scheme is to:

... provide transitional assistance to encourage competitive investment and innovation in the Australian automotive industry in order to achieve sustainable growth, both in the Australian market and internationally, in the context of trade liberalisation.<sup>56</sup>

5.2 The ANAO reviewed DIISR's arrangements for determining whether the Scheme is achieving its objective and how the department reports the Scheme's performance.

### Internal management arrangements

5.3 In DIISR, AusIndustry is responsible for the delivery of ACIS, while the Manufacturing division<sup>57</sup> is responsible, among other things, for:

- providing policy advice and briefings on ACIS to the Minister;
- evaluating the appropriateness and effectiveness of the Scheme; and
- consulting with AusIndustry, and external stakeholders, on any policy and legislative changes to the Scheme.

5.4 Since the ANAO's previous audit of ACIS in 2002–03, the department has discontinued its practice of developing Business Partnerships Agreements between AusIndustry and the relevant policy area—in this case, the Manufacturing division. The agreements were established to provide an understanding of the roles and responsibilities between program design and program delivery. However, other mechanisms have been put in place to monitor and review ACIS (and other programs). These include:

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<sup>56</sup> Section 3 of the *ACIS Administration Act 1999*.

<sup>57</sup> Previously known as the Manufacturing, Engineering and Construction division.

- regular meetings between AusIndustry and other divisions, including Manufacturing, to discuss key issues relating to program performance;
- monthly and quarterly reporting of program performance in AusIndustry, which informs wider departmental reporting; and
- annual customer and stakeholder satisfaction surveys to monitor key aspects of performance.

5.5 In addition to these arrangements, AusIndustry produces a number of internal documents, intended to promote the effective delivery of the Scheme. These include: an annual product plan, which outlines priorities for the Scheme and identifies planned improvements in certain areas such as service delivery; and an annual risk management summary, which identifies key risks to the successful delivery of the Scheme. The risk management summary interlinks with AusIndustry's division-wide risk management plan.

## Measuring the Scheme's performance

5.6 In the department's Outcomes and Outputs Framework for 2005–06, ACIS was included under Outcome 1<sup>58</sup>, and was reported under Output 1.1, Program Management Services. The department's annual report for 2005–06 reported the value of concessions delivered under ACIS as \$486.5 million, for 242 customers.

5.7 The ANAO's previous audit of ACIS noted that, when the Scheme was originally introduced, it was one part of the Government's package of assistance to the automotive industry.<sup>59</sup> While objectives were provided for the overall package of measures, the audit found there were no specific measures for ACIS, nor intermediate outcomes that would indicate how the Scheme contributes towards the Government's overall objectives. To address this issue, the audit recommended that:

...DITR develop appropriate objectives, related intermediate outcomes and associated performance measures for ACIS, to assist in the administration and evaluation of the program, to better inform decision-making, and to enhance accountability.<sup>60</sup>

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<sup>58</sup> 'A stronger, sustainable and internationally competitive Australian industry, comprising the manufacturing, resources and services sector'.

<sup>59</sup> Other parts of the assistance package were the now defunct Automotive Market Access and Development Strategy, and staged reductions to tariffs on passenger motor vehicles.

<sup>60</sup> See Recommendation No. 2 from ANAO, op. cit., p. 39.

## Achievement of intermediate outcomes

5.8 In response to the ANAO's recommendation, the department completed an Intermediate Outcome Performance Report in 2004. The report examined data on performance indicators for three key intermediate outcomes, relating to ACIS Stage 1. A summary of the report's findings is provided in Table 5.1.

**Table 5.1**

### Summary of key performance indicators for ACIS Stage 1

Intermediate outcome	Performance indicator
Sustainable growth of the Australian automotive industry	<ul style="list-style-type: none"> <li>The industry experienced record sales in 2002 and 2003.</li> <li>Local market share of domestic producers has grown slightly since 2001.</li> <li>Motor vehicle producers' sales have increased in value by 61 per cent, and production levels have increased by 17 per cent over the period 1999 to 2003.</li> </ul>
Improved competitiveness of Australian made automotive products and services in the context of trade liberalisation	<ul style="list-style-type: none"> <li>Motor vehicles on the Australian market have become 12.4 per cent more affordable over the period 1996 to 2002, and more affordable compared to the aggregate consumer price index.</li> </ul>
Increase in the level of investment in the Australian automotive industry	<ul style="list-style-type: none"> <li>Investment in plant and equipment increased by 148 per cent over the period 1999 to 2003.</li> <li>Investment in R&amp;D increased by 63 per cent over the period 1999 to 2003.</li> </ul>

Source: Department of Innovation, Industry, Science and Research

5.9 The Intermediate Outcomes Report stated that, while it may be some years after 2005 before it is known whether Stage 1 has achieved its purposes (partly due to the tariff reductions happening that year), analysis of key performance indicators suggests that the intermediate outcomes are likely to be achieved.<sup>61</sup>

5.10 DIISR advised the ANAO that it intends evaluating the performance of ACIS again in 2009, one year before the end of Stage 2. It also noted that the Productivity Commission's (second) review of government assistance to the automotive sector is scheduled for 2008. As with the first review, which was conducted during Stage 1 of the Scheme<sup>62</sup>, the second review is expected to

<sup>61</sup> DIISR noted, however, that the report was not a substitute for an evaluation of ACIS and should not be interpreted in isolation from the broader context of factors impacting upon the automotive community.

<sup>62</sup> The Commission's *Review of Automotive Assistance*, published in August 2002, made a number of findings to assist the Government to determine policy options for the automotive sector.

provide an external assessment of the broader environment facing the automotive sector.

## **Outputs**

5.11 The main output of ACIS is the number of duty credits issued to Scheme participants. As previously noted, some 99 per cent of the duty credits from the \$2 billion capped funding pool for Stage 1 were issued to participants. Moreover, the demand for duty credits in both Stage 1 and Stage 2 (to date) has exceeded the number of credits available to be issued to participants, requiring the credits to be modulated.

5.12 The strong demand for ACIS duty credits suggests that the Scheme has been effectively promoted within the automotive industry, and is providing an incentive to companies to invest in new capital equipment and R&D, to help make their operations more competitive and sustainable.

## **Reporting on the Scheme's outcomes and outputs**

5.13 Although DIISR collects data on outputs and intermediate outcomes for ACIS, only limited performance information has been provided to external stakeholders, including the Parliament. For example, the department's last three annual reports provided descriptive information on the Scheme only. The report did not provide a breakdown of the duty credits issued to the supply chain sectors or to individual MVPs; nor did the more recent annual reports present any of DIISR's analysis of intermediate outcomes from its 2004 internal report. Moreover, this type of information has not been made publicly available elsewhere, for example in media releases or on the department's website.

## **'Commercial-in-confidence' issues**

5.14 DIISR acknowledged that only limited performance information on ACIS has been made public. It advised the ANAO that for Stage 2 the Act provides the Minister with the discretion to decide whether to publish information relating to ACIS participants (for example the number of duty credits received by each MVP or supply chain participant); and the then Minister had decided not to publish these details.

5.15 Also, during Stage 1, DIISR provided participants with an undertaking that the information provided in their registration and quarterly return forms would be treated as 'commercial-in-confidence'. However, DIISR

acknowledged that there was no specific statutory source for this undertaking. That is, there was no legislative requirement precluding the department from reporting publicly on the number and type of credits issued to participants during this stage.

5.16 The ANAO recognises that there may be commercial sensitivities involved in publicly disclosing the number of duty credits issued to individual Scheme participants. However, since ACIS is the Government's key assistance measure for the automotive industry, and is the department's largest administered program, the ANAO considers that the department has an obligation to inform stakeholders, especially the Parliament, on how the Scheme is progressing. As a minimum, this should include reporting publicly, in aggregate terms, on the number of credits issued to MVPs and supply chain participants; and on the volume of production and investment activities that such entities have engaged in to receive duty credits. Further, information on intermediate outcomes should also be provided following the evaluation of the Scheme, planned for 2009.

5.17 The ANAO also considers that DIISR should report the results of its compliance activities on ACIS, to better inform stakeholders on the integrity of participants' claims and its stewardship of public funds.

## Conclusion

5.18 In 2004, the department assessed whether the intended outcomes for ACIS were being achieved, and early indications were that the Scheme is helping to promote a more competitive and sustainable automotive industry in Australia. Although data on intermediate outcomes and annual outputs is being collected, only limited information has been reported publicly for the benefit of external stakeholders, including the Parliament.

5.19 The ANAO recognises that the department has concerns about the commercial sensitivities involved in reporting publicly on aspects of ACIS. However, given that ACIS is the Government's key assistance measure for the automotive industry and involves a substantial level of government support, there is scope to provide greater disclosure of the duty credits issued to Scheme participants.

## Recommendation No.3

5.20 The ANAO recommends that the Department of Innovation, Industry, Science and Research enhance the level of public reporting on the Automotive Competitiveness and Investment Scheme, including:

- (a) the aggregate number of duty credits issued to motor vehicle producers and the three supply chain sectors;
- (b) the broad results of compliance activities; and
- (c) progress against intermediate outcomes, as data becomes available.

### DIISR's response

5.21 Agreed. The department acknowledges the ANAO's view that there should be more public reporting on the program. The department will report annually on aggregate duty credits issued to each of the four industry sectors covered by the scheme and also agrees to report progress against intermediate outcomes in 2009, following the review of automotive arrangements scheduled for 2008. The department also sees merit in publicly reporting the broad outcomes of compliance actions on an annual basis.

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Ian McPhee  
Auditor-General

Canberra ACT  
22 January 2008

# Appendices





## Appendix 1: DIISR and Customs' full response to this audit

Secretary

Mr Peter McVay  
Acting Executive Director  
Performance Audit Services Group  
Australian National Audit Office  
GO Box 707  
Canberra ACT 2601



**Australian Government**  
**Department of Innovation  
Industry, Science and Research**

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ABN: 74 599 608 295

Dear Mr McVay

### **ANAO Performance Audit – Administration of the Automotive Competitiveness and Investment Scheme**

I refer to your letter of 20 November 2007, concerning the Australian National Audit Office (ANAO) draft report on Administration of the Automotive Competitiveness and Investment Scheme.

The Department's full response and detailed responses to the recommendations are highlighted in Attachment A. The summary response for use in the preparation of the audit report brochure is provided in Attachment B.

Should you have any further queries in relation to this response, please contact Mrs Lisa Hind, Chief Internal Auditor on 02 6213 6471.

Yours sincerely

A handwritten signature in black ink that reads "Mark I Paterson".

Mark I Paterson AO

12 December 2007

**Department's Full Response to the Audit**

The department notes the ANAO's conclusion that it has established a sound control framework to facilitate compliance with legislative requirements and to manage financial risks when issuing credits in the ACIS scheme. In addition the ANAO has indicated that the department has well-developed processes in place to assess the eligibility of scheme participants to receive credits and to accurately calculate individual claims while ensuring adherence to the funding limits of the scheme. Further, the ANAO has found that the department has implemented appropriate processes to manage the allocation of credits under the \$150M MVP R&D Scheme.

The department acknowledges the ANAO's view that there should be more public reporting on the program. The department will report annually on aggregate duty credits issued to each of the four industry sectors covered by the scheme and also agrees to report progress against intermediate outcomes in 2009, following the review of automotive arrangements scheduled for 2008. The department also sees merit in publicly reporting the broad outcomes of compliance actions on an annual basis.

The ANAO has also recommended changes to the current compliance regime for the scheme to enhance the targeting of compliance actions. The department's compliance activities are based on a sound risk management approach. All scheme participants are actively monitored at the quarterly return stage and the department conducts detailed audits of participants rated medium and high risk. To date all high risk participants and all but one medium risk participant have been audited. While the department takes into account audit outcomes in risk rating scheme participants and in targeting its audits, it sees merit in placing the analysis of compliance outcomes on a more systematic basis. Design of a formal, systematic approach to analysing audit outcomes was underway before the ANAO audit commenced and is expected to be completed soon.

The department notes the ANAO's finding that Customs and the department have workable arrangements in place to manage and transfer credits in a timely and secure manner. The department agrees that documentation and processes around reconciling the ACIS records of the two agencies can be improved. It is expected that this will be in place early in the new calendar year.

**A Response to each of the Recommendations****Recommendation 1**

*The ANAO recommends that the Department of Industry, Tourism and Resources systematically analyse and use the results of compliance activities of the Automotive Competitiveness and Investment Scheme to:*

- (a) inform its approach to promoting accurate claiming by Scheme participants; and*
- (b) determine the coverage and scope of future compliance audits*

**Department Response**

Agreed. The department's compliance activities covering scheme participants are based on a sound risk management approach. All participants are actively monitored at the quarterly return stage and the department conducts detailed audits of scheme participants rated medium and high risk. To date all high risk participants and all but one medium risk participant have been audited. While the department takes into account audit outcomes in risk rating scheme participants and in targeting its audits, it sees merit in placing the analysis of compliance outcomes on a more systematic basis. Design of a formal, systematic approach to analysing audit outcomes was underway before the ANAO audit commenced and is expected to be completed soon.

**Recommendation 2**

*The ANAO recommends that the Department of Industry, Tourism and Resources and the Australian Customs Service review their governance arrangements, and document procedures to support their respective responsibilities for managing the transfer, use and reporting of duty credits under the Automotive Competitiveness and Investment Scheme.*

**Department Response**

Agreed. The department notes the ANAO's finding that Customs and the department have workable arrangements in place to manage and transfer credits in a timely and secure manner. The department agrees that documentation and processes around reconciling the ACIS records of the two agencies can be improved. It is expected that this will be in place early in the new calendar year.

**Recommendation 3**

*The ANAO recommends that the Department of Industry, Tourism and Resources enhance the level of public reporting on the Automotive Competitiveness and Investment Scheme, including:*

- (a) the aggregate number of duty credits issued to motor vehicle producers and the three supply chain sectors;*
- (b) the broad results of compliance activities; and*
- (c) progress against intermediate outcomes, as data become available.*

**Department Response**

Agreed. The department acknowledges the ANAO's view that there should be more public reporting on the program. The department will report annually on aggregate duty credits issued to each of the four industry sectors covered by the scheme and also agrees to report progress against intermediate outcomes in 2009, following the review of automotive arrangements scheduled for 2008. The department also sees merit in publicly reporting the broad outcomes of compliance actions on an annual basis.

**ATTACHMENT B****Summary of Department's Response to this Audit**

The department notes the ANAO's conclusion that it has established a sound control framework to facilitate compliance with legislative requirements and to manage financial risks when issuing credits in the ACIS scheme. In addition the ANAO has indicated that the department has well-developed processes in place to assess the eligibility of scheme participants to receive credits and to accurately calculate individual claims while ensuring adherence to the funding limits of the scheme. Further, the ANAO has found that the department has implemented appropriate processes to manage the allocation of credits under the \$150M MVP R&D Scheme. The department accepts the recommendation to provide more public reporting; the recommendation to enhance its targeting of compliance actions and the recommendation to upgrade its credit reconciliation processes with Customs.



Ms Barbara Cass  
Executive Director  
Performance Audit Services Group  
Australian National Audit Office  
GPO Box 707  
CANBERRA ACT 2601

Dear Barbara

Thank you for the opportunity to comment on those parts of the draft performance audit on administration of the Automotive Competitiveness Investment Scheme (ACIS) that make reference to Customs (introductory chapter and chapter 4).

Customs appreciates that the audit report represents the outcome of a thorough examination of management processes governing the administration of ACIS. Customs notes the ANAO conclusion that Customs has a sound control framework to ensure that duty credits are used only in relation to eligible imports and that a more comprehensive reconciliation process is now being put in place between DITR and Customs. Customs agrees with the ANAO's recommendation in relation to the governance arrangements and procedures to support the management of the transfer, use and reporting of duty credits under the ACIS.

Customs provides the following formal response to the performance audit report.

#### **Customs Full Response to Audit**

Customs notes the ANAO finding that Customs has a sound framework to manage the use of ACIS credits for eligible imports. Similarly, the ANAO found that Customs controls over the payment of ACIS refunds, and refunds generally, are satisfactory.

Customs agrees that the documentation and processes for reconciling ACIS records could be improved and is working with DITR to this end. This will align with the outcome of the 'system under development' internal audit review that Customs commissioned in 2007 to document and provide quality and audit controls in respect of manual intervention, if it is required in the future.

#### **Recommendation 2**

*The ANAO recommends that the Department of Industry, Tourism and Resources and the Australian Customs Service review their governance arrangements, and document procedures to support their respective responsibilities for managing the transfer, use and reporting of duty credits under the Automotive Competitiveness and Investment Scheme.*

Agreed.

Customs recognises the need to update and further develop procedural documentation with DITR to ensure that the responsibilities of each agency are more clearly defined. The current documents and processes between Customs and DITR are being revised and are expected to be finalised in early 2008.

**Summary of Customs response**

Customs notes the ANAO finding that Customs has a sound framework to manage the use of ACIS credits for eligible imports. Similarly, the ANAO found that Customs controls over the payment of ACIS refunds, and refunds generally, are satisfactory.

Customs recognises the need to update and further develop procedural documentation with DITR to ensure that the responsibilities of each agency are more clearly defined.



Sue Pitman  
National Director Trade  
Australian Customs Service

17 December 2007

## Appendix 2: Status of recommendations from the ANAO's 2002–03 audit of ACIS<sup>63</sup>

Previous recommendation and agency response	Current status
<p><b>Recommendation No. 1</b></p> <p>The ANAO recommends that, in order to ensure a clear understanding of roles, responsibilities and procedural requirements and standards, DITR promptly finalise:</p> <ul style="list-style-type: none"> <li>• the MoU with Customs; and</li> <li>• a procedures manual for the scheme.</li> </ul> <p><b>DITR response: Agreed</b> <b>Customs response: Agreed</b></p>	<p><b>Implemented.</b> MoU and procedures manual in place. See paragraphs 1.18 and 2.8.</p>
<p><b>Recommendation No. 2</b></p> <p>The ANAO recommends that DITR develop appropriate objectives, related intermediate outcomes and associated performance measures for ACIS, to assist in the administration and evaluation of the program, to better inform decision making, and to enhance accountability.</p> <p><b>DITR response: Agreed</b></p>	<p><b>Partially implemented.</b></p> <p>Intermediate Outcomes Performance Report produced in 2004; and a further evaluation is scheduled for 2009. However, only limited information has been made available for the benefit of external stakeholders, including the Parliament.</p> <p>See paragraphs 5.8 to 5.10.</p>
<p><b>Recommendation No. 3</b></p> <p>The ANAO recommends that DITR develop a structured risk management plan for ACIS, including provisions for regular monitoring and review. Risk management arrangements should include provision in the MoU with Customs for sharing information on risk management.</p> <p><b>DITR response: Agreed</b> <b>Customs response: Agreed</b></p>	<p><b>Partially implemented.</b></p> <p>Annual risk management summary in place, but the MoU does not explicitly address sharing of information. Further, joint procedures have not been developed by DIISR and Customs to support their administration of ACIS.</p> <p>See paragraphs 4.28 to 4.31.</p>
<p><b>Recommendation No. 4</b></p> <p>The ANAO recommends that DITR review its registration processes and ensure that they are consistent with its obligations under the <i>ACIS Administration Act 1999</i>.</p> <p><b>DITR response: Agreed</b></p>	<p><b>Implemented.</b></p> <p>A procedures manual and a registration checklist were finalised in October 2003. See paragraphs 2.7 to 2.8.</p>
<p><b>Recommendation No. 5</b></p> <p>The ANAO recommends that DITR ensure that forecasts and estimates supporting advice in designing industry support schemes are updated as design parameters and the program environment change, and as more data becomes available.</p> <p><b>DITR response: Agreed</b></p>	<p><b>Not applicable.</b></p> <p>This recommendation was not examined as did not relate directly to the delivery of ACIS Stage 2.</p>

<sup>63</sup> ANAO, op. cit., pp. 21–24.

Previous recommendation and agency response	Current status
<p><b>Recommendation No. 6</b></p> <p>The ANAO recommends that AusIndustry implement procedures and guidelines to establish a standard approach to auditing compliance consistent with its legislative obligations and program risks. Such an approach includes:</p> <ul style="list-style-type: none"> <li>• clearly articulated standards, procedures and supporting methodologies (such as audit sampling tools);</li> <li>• appropriate audit documentation and planning;</li> <li>• identifying required skills/competencies and the means of achieving them; and ensuring compliance with legislative requirements.</li> </ul> <p><b>DITR response: Agreed</b></p>	<p><b>Implemented.</b></p> <p><i>Risk and Audit Handbook</i> issued in July 2003, which includes guidance on audit planning and audit sampling. A specialist audit team has also been established. See paragraphs 3.14 to 3.15.</p>

Source: ANAO



## Appendix 3: Accounting treatment for ACIS duty credits

In 2005–06, the accounting treatment for ACIS duty credits was changed in the department's and in Customs' financial statements to better reflect the nature of the transactions and DIISR's key role in administering the Scheme. The current accounting treatment is summarised below.

### **DIISR**

- When duty credits issued to Scheme participants, they are recognised as an Administered expense and an Administered liability.
- When duty credits are used at Customs to offset the duty payable on eligible imports, they reduce the Administered liability for that period, and the use of the credits are now accounted for as a movement through equity, rather than as Administered revenue, as happened prior to 2005–06.
- Duty credits that have been issued to, but not used by Scheme participants, are recorded as an Administered liability, as these credits have ongoing value and are valid until they expire at the end of each ACIS stage. For example, duty credits issued during Stage 2 can be used until 31 December 2011.

### **Customs**

- When duty credits are used to offset the duty on eligible imports, they are now recognised as Administered resources transferred between government agencies, rather than as an Administered expense, as happened prior to 2005–06.

Source: ANAO



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