

The Auditor-General
Audit Report No.12 2002-03
Performance Audit

Management of the Innovation Investment Fund Program

**Department of Industry, Tourism and Resources
Industry Research and Development Board**

Australian National Audit Office



Canberra ACT
21 October 2002

Dear Mr President
Dear Mr Speaker

The Australian National Audit Office has undertaken a performance audit in the Department of Industry, Tourism and Resources and the Industry Research and Development Board in accordance with the authority contained in the *Auditor-General Act 1997*. I present this report of this audit, and the accompanying brochure, to the Parliament. The report is titled *Management of the Innovation Investment Fund Program*.

Following its tabling in Parliament, 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
Acting Auditor-General

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

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Summary and Recommendations

Audit Findings and Conclusions

Figure 2.1
IIF Accountabilities and Reporting Structures

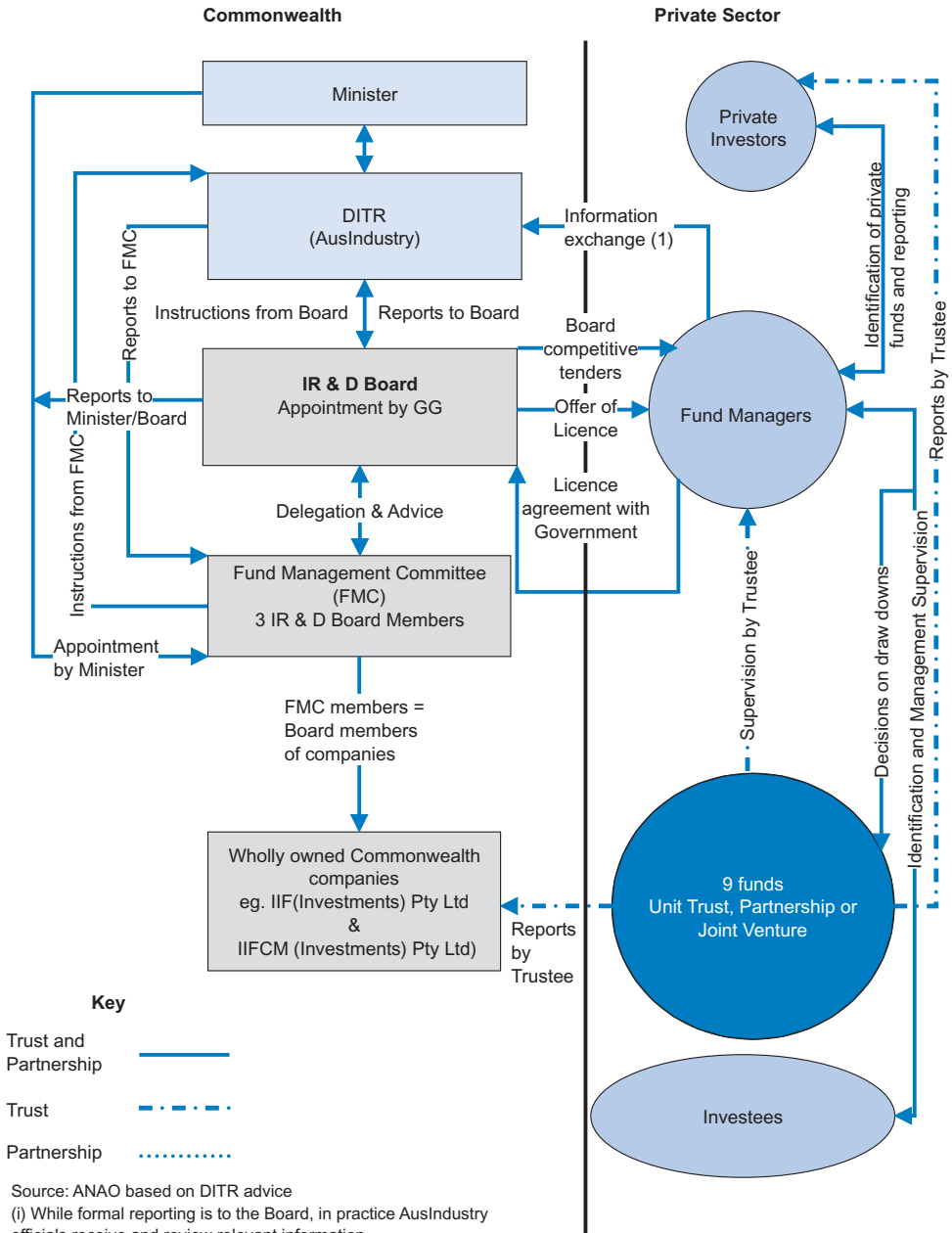
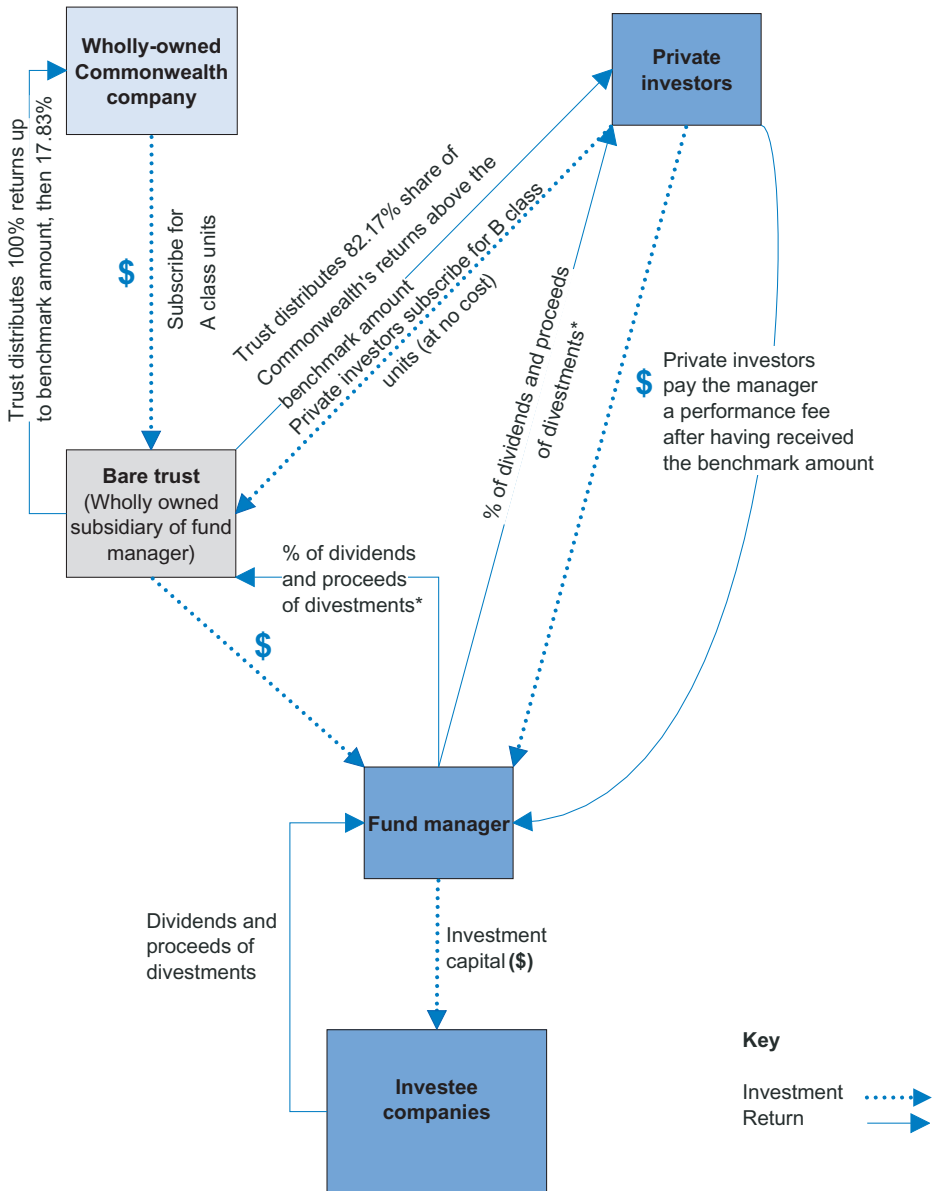


Figure 3.1

Round 2 direct investment arrangement: investment and distribution flows



Note: - * The percentage of dividends and proceeds of divestments returned to trust and private investors in line with percentage invested from these sources of total capital.

Source: Department of Industry Tourism and Resources.

Table 5.1**Reporting by fund managers to the IR&D Board**

Type	Contractual requirement	Audit finding
Financial reports	Annual audited financial statement required: within three months of the end of the financial year for Round 1 fund managers ⁶⁹ ; and within 60 days of the end of the financial year for Round 2 fund managers. Unaudited financial statement required at the end of the calendar year.	Reports have generally been submitted on time, and in the required format. Late reports have been submitted soon after the required dates.
Valuation of investments	Valuations of investments in the investee companies based on Australian Venture Capital Association Limited methodology: ⁷⁰ —at the at the end of the financial year with the valuations signed off by the funds' external auditors; and—at the end of the calendar year.	Valuations were submitted with the financial statements.
Economic impact statements of investments	Economic impact statements are required as part of end-of-financial-year reporting. Information reported relates to: —export and domestic sales; —import replacement activities; —employment growth (direct and indirect); —revenue growth; and —product development and commercialisation in relation to each investee company.	These statements were submitted with end-of-financial-year financial statements. There are wide discrepancies in the sales figures reported by two different fund managers from a single company in which both invest, as there has been no guidance on how the results should be determined. AusIndustry has advised the ANAO that it will clarify reporting requirements for fund managers to ensure consistency in the future.

Source: Licence agreements between IR&D Board and fund managers; and ANAO analysis of reports from fund managers.

⁶⁹ The Ministerial Directions to the Board for developing the program guidelines for Round 1 specify that these reports must be audited by the Commonwealth Auditor-General or an auditor approved by the Commonwealth Auditor-General. DITR has advised that, as a result of discussions with the selected fund managers, the FMC concluded that the use of the fund manager's existing auditor could provide equivalent levels of assurance in regard to the fund's financial statements. The Ministerial Directions to the Board for Round 2 does not include this requirement.

⁷⁰ The Australian Venture Capital Association Limited has recommended that the valuation of early stage investments is to be at cost, based on the last investment in the company, unless there is a prima facie indicator that value should be written down. In the Round One 1 licence agreements, the fund managers were required to use an independent valuer approved by the IR&D Board to provide the end-of-financial-year reports to the Board. However, in mid-1999, the FMC reconsidered these requirements for valuation, as this approach was considered costly and was not required for investor protection. The IR&D Board changed the requirement to the current approach, in line with the FMC's recommendation.

Appendices

Appendix 3

Partnership and Unit Trust Arrangements

Figure A3.1

Diagram of typical partnership arrangement

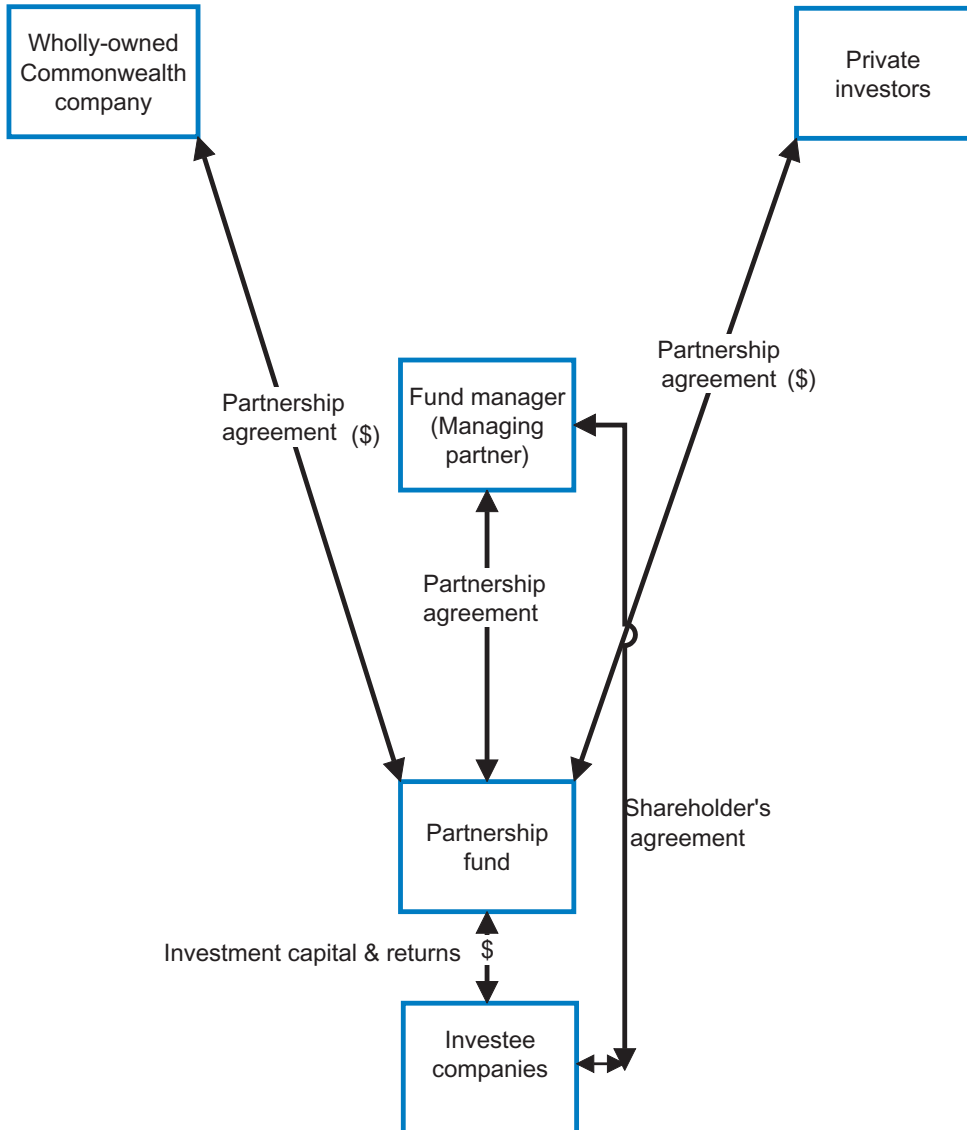
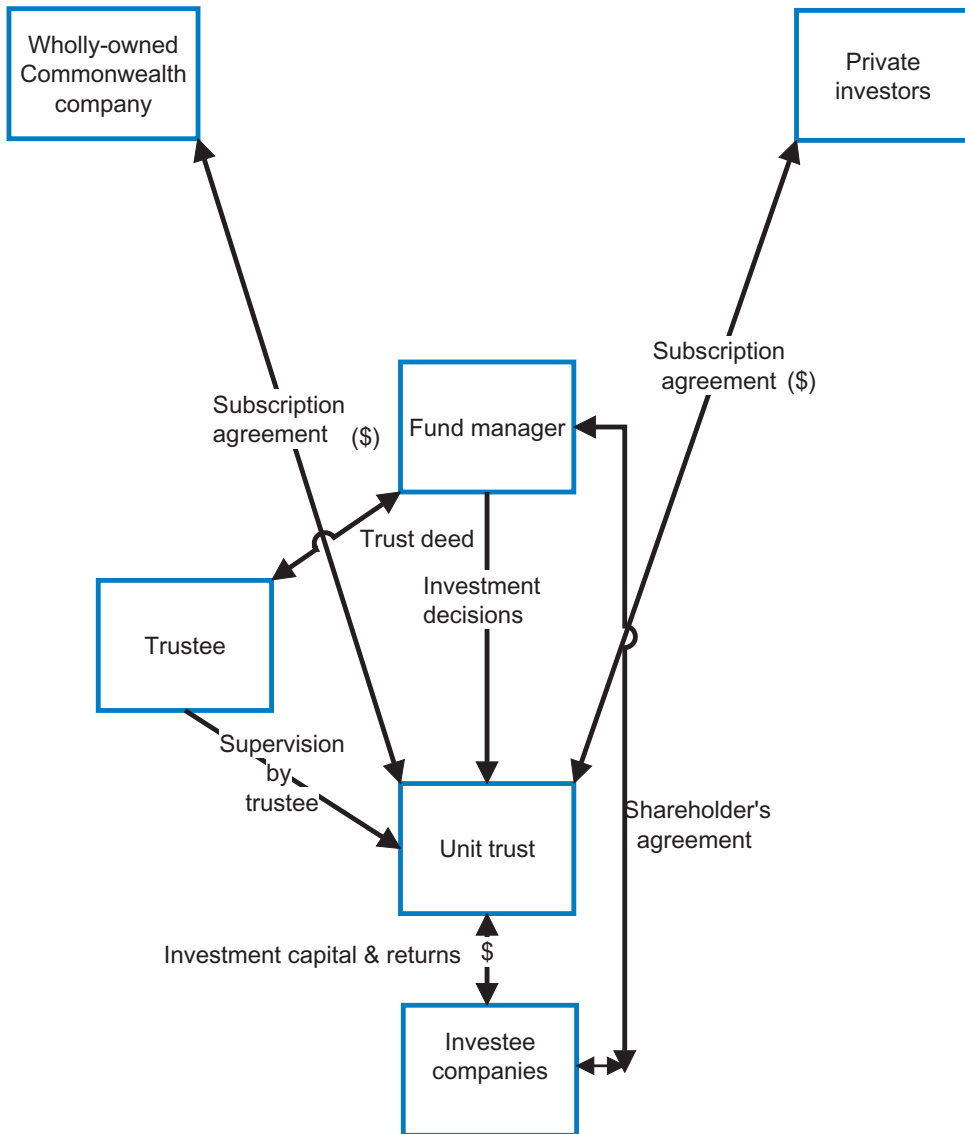


Figure A3.2
Diagram of typical unit trust arrangement



Appendix 4

Investments and Returns - Processes

Figure A4.1

Flows for investments and returns for IIF monies.

