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PARLIAMENT OF TASMANIA

**AUDITOR-GENERAL
SPECIAL REPORT No. 32**

ASSISTANCE TO INDUSTRY

July 2000

*Presented to both Houses of Parliament in accordance with the provisions of Section 57 of
the Financial Management and Audit Act 1990*

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5 July 2000

President
Legislative Council
HOBART

Speaker
House of Assembly
HOBART

Dear Mr President
Dear Mr Speaker

PERFORMANCE AUDIT NO 32.
ASSISTANCE TO INDUSTRY

This report has been prepared consequent to examinations conducted under Section 44 of the *Financial Management and Audit Act 1990*, for submission to Parliament under the provisions of Section 57 of the Act.

Performance audits seek to provide Parliament with assessments of the effectiveness and efficiency of public sector programs and activities, thereby identifying opportunities for improved performance.

The information provided through this approach will, I am sure, assist Parliament in better evaluating agency performance and enhance Parliamentary decision making to the benefit of all Tasmanians.

Yours sincerely

D W R Baulch
ACTING AUDITOR-GENERAL

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LIST OF ACRONYMS AND ABBREVIATIONS

| | |
|----------|---|
| BEC | Business Enterprise Centre |
| CCIAS | Call Centre Investment Attraction Strategy |
| DPAC | Department of Premier and Cabinet |
| DSD | Department of State Development |
| IDP | Industry Development Plan |
| ITD | Investment, Trade and Development |
| LEI | Local Employment Initiatives |
| MPT | Major Projects Team |
| NCP | National Competition Policy |
| NPV | Net Present Value |
| PI | Performance Indicator |
| SWOT | Strengths, weaknesses, opportunities, threats |
| TDR | Tasmania Development and Resources |
| Treasury | Department of Treasury and Finance |

INTRODUCTION

Under the provisions of section 44(b) of the *Financial Management and Audit Act 1990* the Auditor-General may

'carry out examinations of the economy, efficiency and effectiveness of Government departments, public bodies or parts of Government departments or public bodies'

The conduct of such audits is often referred to as performance auditing. This report relates to a performance audit carried out by the Tasmanian Audit Office during the period November 1999 to January 2000 on assistance to industry made available through the Department of State Development (DSD).

The objective of this audit was to assess the effectiveness of the Department's management of assistance to industry.

The approach taken by the Audit Office was to examine the procedures used during each phase of the assistance process for a selection of assistance payments made between 1997 and 1999. For the purposes of this report the term "assistance" is used as shorthand for "assistance to industry".

As well, in regard to DSD's Local Employment Initiatives program, three Business Enterprise Centres were examined in respect of strategic planning, consistency with DSD's program guidelines and performance management.

AUDIT OPINION

| | |
|--------------------------------------|--|
| Report Title | Assistance to Industry |
| Nature of the Audit | The objective of this performance audit was to assess the effectiveness of management of assistance to industry processes as undertaken by the Department of State Development (DSD). |
| Responsible Party | Head of Agency for the Department of State Development. |
| Mandate | <p>This audit has been carried out under the provisions of Section 44(b) of the <i>Financial Management and Audit Act 1990</i> which provides that:</p> <p><i>“The Auditor-General may carry out examinations of the economy, efficiency and effectiveness of Government departments, public bodies or parts of Government department or public bodies.”</i></p> |
| Applicable Standards | <p>This audit has been performed in accordance with Australian Auditing Standard AUS 806 “Performance Auditing” which states that:</p> <p><i>“The objective of a performance audit is to enable the auditor to express an opinion whether, in all material respects, all or part of an entity’s activities have been carried out economically, and/or efficiently and/or effectively.”</i></p> |
| Limitation on Audit Assurance | Audit procedures were restricted to testing of a limited number of assistance packages and Business Enterprise Centres. This provides less evidence than would be available by applying more extensive and comprehensive procedures. The evidence provided by these means is persuasive rather than conclusive in nature. |
| Audit Criteria | <p>The effectiveness and efficiency of management of assistance to industry was ascertained under the following criteria:</p> <ul style="list-style-type: none"> ?? <i>Whether the assistance achieved its objective;</i> ?? <i>Requests for assistance are made by proponents of projects where the decision to proceed is likely to be dependent on the provision of incentives;</i> ?? <i>DSD’s assessment mechanisms enable the Department to determine the maximum level of incentive which could be provided;</i> ?? <i>The Department provides no more incentives than are necessary to attract or retain desired projects; and</i> ?? <i>The Department has effective mechanisms in place to ensure accountability for any incentives provided.</i> <p>Business Enterprise Centres (BECs) were reviewed in relation to the following criteria:</p> <ul style="list-style-type: none"> ?? <i>The strategic plans used contain achievable and measurable targets and are linked to annual plans and regular performance reports; and</i> |

?? BECs comply with DSD's Guidelines for the Local Employment Initiatives (LEI) in regard to governance structures, the facilitator's role, and annual reporting.

**Opinion and
Conclusions**

On the basis of the limited sample of assistance packages examined, DSD's assistance to industry has been effective in achieving the desired outcome, which in nearly all cases was the creation or maintenance of employment.

It is probable that the projects in the sample, and in particular the call centres, would not have proceeded in the absence of the assistance.

The maximum level of assistance offered by DSD is determined by a Board policy that was developed in relation to call centres but in practice appears to apply to all assistance. The policy limits the Net Present Value of assistance to a project on a cost per job basis. However, in the case of a guarantee extended for one project in the sample, the assistance taken together with previous assistance over a long period, would have comfortably exceeded the current limit.

The DSD records of negotiations were not sufficiently detailed to enable an opinion to be given on whether the minimum incentive sufficient to attract/retain the project was provided. Nevertheless, internal review and approval processes would tend to ensure this outcome.

DSD has effective mechanisms to ensure accountability for any incentives provided.

In relation to the sample of BECs:

- ?? Each BEC had a strategic plan and was providing regular performance reports; and
- ?? Each BEC had an approved form of governance structure and provided annual reporting.

DEPARTMENTAL RESPONSE

Much of the audit relies on a series of comparisons or benchmarks that are taken from two other studies, AONSW 1998 Department of State and Regional Development – Provision of Industry Assistance, Sydney: Government Printer and the Industry Commission report 1996, State, Territory and Local Government Assistance to Industry, Report No 55: Australian Government Publishing Service. The Performance Audit accepts as given the authority, validity, relevance and currency of these reports without questioning any of these issues. This leaves the audit flawed. It is, in effect, making comparisons and using benchmarks that have never been tested for appropriateness.

As an example, the 1996 Industry Commission report was developed as a general document with the objective of developing holistic recommendations Australia wide. It is an undeniable fact that States, Territories and Local Government compete for development and that applying such guidelines to Tasmania alone would place us at a significant competitive disadvantage.

Furthermore, there has been no questioning of the motives of this Federal Government agency policy, ostensibly driven by a national government with a different political agenda, different policy objectives and a different perspective on the issues at hand.

No consideration has been given to Tasmanian government policy.

I would point out that this is not a matter of mere semantics, it is a clear tenet of management, particularly management by objectives, that individuals and organisations move towards what is being measured. This report is clearly capable of having this effect without any questioning of the validity of the stated benchmarks.

I would also point out that the information-gathering stage of this report was conducted half a decade ago and, since that time, there has been considerable change in the national economic outlook and the economic outlook for Tasmania.

For these reasons I do not accept the Industry Commission's report as being an appropriate yardstick and, similarly, I do not accept that the NSW Auditor General's report should have any authority, persuasive or otherwise, over the performance of the Department of State Development in Tasmania.

SUMMARY OF AUDIT RECOMMENDATIONS

In addition to the cost per job benchmark DSD should consider using a basis of evaluation of major projects for assistance (e.g. where the aid will exceed \$1M) that includes analysis of benefits to the State, as well as reflecting all related costs.

Page 19

DSD should produce its own departmental guidelines on the administration of assistance.

The Board paper template should include a section dealing with the potential risks and exposures relating to proposed project assistance.

Page 22

Assistance to industry files should contain complete documentation to allow straightforward examination of projects and to ensure transparency of management processes.

Page 24

The issue of commercial confidentiality should not take precedence over governmental accountability and DSD should document the rationale for all decisions made during the negotiation stage.

Page 25

There should be public disclosure regarding firms or projects receiving government assistance and details of benefits provided.

Page 26

AUDIT OBJECTIVE, APPROACH AND COST

Audit Objective

The objective of this audit was to assess the effectiveness and efficiency of management of assistance to industry processes as undertaken by the DSD which has primary responsibility for this area. Aspects examined included various stages of assistance, including the methodology in developing overall assistance strategies, the degree of transparency and accountability present in the pre-proposal, assessment and negotiation stages, and post-award monitoring and evaluation of individual recipients and related programs. This assessment was carried out in regard to the following audit criteria:

- ?? The assistance provided achieved its objective - usually that of creating or maintaining employment;
 - ?? Requests for assistance are made by proponents of projects where the decision to proceed is likely to be dependent on the provision of incentives;
 - ?? DSD's assessment mechanisms enable the Department to determine the maximum and appropriate level of incentive which could be provided;
 - ?? The Department provides no more incentives than are necessary to attract or retain desired projects; and
 - ?? DSD has effective mechanisms in place to ensure accountability for any incentives provided.
- These criteria are discussed in more detail below.

Scope of the Audit

The Audit Office restricted its testing to a selection of assistance payments made between July 1996 and December 1999 and examined call centre assistance packages as well as guarantees, accommodation incentives and general assistance. We also reviewed the Local Employment Initiatives (LEI) program in detail, reviewing DSD's guidelines for this program, as well as three Business Enterprise Centres (BECs) which received assistance during the 1998-99 year.

It should be noted that this audit did not address broad issues of policy, such as appropriateness of one particular program over another, but did examine the approach used by the Department to develop its assistance programs.

Audit Criteria

The Audit Office examined payments made in relation to 19 companies or projects over the three-year period referred to above against best practice standards noted in a 1998 report by the Audit Office of New South Wales titled *Department of State and Regional Development – Provision of Industry Assistance*. In that report, payments of assistance were examined under four stages of the process, as follows:

- ?? Pre-Proposal Stage – This phase covers the planning and design of an assistance program, such as agreement on the objectives of the program, identification of targeted industries and research into what affected companies perceive to be useful incentives, together with selection criteria, negotiation leverage, publication and dissemination of promotional materials. An overall strategy for the program is also formulated, including timelines for reviews and evaluations. After such 'background' work is undertaken, proponents should be

able to find out enough information about the particular assistance to determine if it is appropriate for their business, due to comprehensive, accurate, and clear documentation, either in print, on the Internet, or by speaking to a Departmental officer. For programs that seek to engage companies to come to the state there needs to be adequate information available to determine which companies are appropriate to contact.

- ?? Assessment Stage – Under the next phase, documented eligibility criteria which are clearly worded assist the Department in assessing either the application made by a proponent, or in formulating a proposed package for a targeted company. Such assessment criteria are consistently implemented for all types of incentives to ensure accountability, and the level of documentation during this stage enhances transparency and equity in decision-making.

The Audit Office also sought to assess how the Department managed assistance to industry whilst observing National Competition Policy (NCP) principles.

There appears to be some variability in the interpretation of NCP principles between the states. The Tasmanian Department of Treasury and Finance, which has primary responsibility for the Government's compliance with NCP considers that the concept of 'competitive neutrality' is confined to issues surrounding government business enterprises. However, as indicated in that State's submission to the Industry Commission, New South Wales took the view that:

'State industry assistance should not breach competitive neutrality for the following reasons: Firstly, on equity grounds, the taxpayer's money should not be used to advantage one enterprise over another. Secondly, on efficiency grounds, assistance which breaches competitive neutrality is likely to direct production away from existing producers in that industry and the net gain in output and employment may be small or zero.'¹

Discussions with DSD officers indicated that these competitive neutrality issues are examined during the assessment process.

- ?? Negotiation Stage – During this period an appraisal of what might be considered an acceptable offer precedes negotiations. Officers in charge of negotiation work within well-defined limits of responsibility to ensure that incentives offered to companies do not exceed the assessed levels to assist the related industry. The stage concludes with a binding written agreement containing achievable yet challenging performance targets for the company, as well as addressing commercial-in-confidence issues and reporting requirements. Such agreements include clawback provisions, where relevant, to ensure that inducements can be recovered in cases of non-performance of all or some of the obligations to be carried out by the business.
- ?? Post Awarding Stage – The final phase involves the provision of incentives consistent with the written agreement, and DSD's monitoring of the contractual performance as well as the business's continued viability to safeguard public funds. Post-assistance evaluation is carried out to gauge the impact of the intervention against the original objectives. The information from such evaluations is then used to improve the assistance program. Stakeholders are provided with sufficient information about DSD's performance to enable them to make a meaningful assessment.

Similarly, in its 1996 report, the Industry Commission considered that clear and open administration procedures for governmental assistance to industry should include:

- ?? Clearly stated objectives which are publicly available, with these objectives specified in a manner that is open to quantification and verification;

¹ Industry Commission. 1996. *State, Territory and Local Government Assistance to Industry*, Report No 55. Canberra: Australian Government Publishing Service, page 63.

-
- ?? Publicly available eligibility criteria, involving minimal discretion and maximum quantifiable criteria;
 - ?? Transparent and open approval processes;
 - ?? Monitoring arrangements;
 - ?? Quantitative performance measures which establish broad targets and qualitative performance measures that clearly relate to the objectives of the assistance program as a means of providing an overall indication of effectiveness;
 - ?? Reporting requirements; and
 - ?? A regular program evaluation process.²

In regard to the Audit Office's examination of BECs, officers compared recommended practices set out in DSD's Guidelines with approaches adopted by three BECs, namely Business East in Bellerive, Southern Enterprise Centre in Glenorchy, and the Derwent Valley Enterprise Centre in New Norfolk. Areas examined included:

- ?? Corporate governance structure including an incorporated entity and a Board of Management comprised of business community stakeholders who have the requisite skills and knowledge to manage the BEC;
- ?? Roles and responsibilities of the BEC's facilitator/manager;
- ?? The existence of a clear strategic plan that is derived from the particular characteristics and needs of the local area, potential opportunities for further development and problems that need to be addressed. The plan should be developed through consultation with local interest groups, with the support of relevant State and Local Government contacts;
- ?? The development of annual plans that link to the strategic plan to ensure the targets are met;
- ?? Quarterly or half-yearly reports setting out the BEC's achievements in regard to jobs created and retained, clients serviced, assistance results, other development activities, and financial data;
- ?? Level of funding provided by DSD and the extent to which it was related to a BEC's previous performance;
- ?? An annual report which not only includes the above indicators, but also reports on the year's progress in achieving the targets, and an audited financial statement; and
- ?? Regular monitoring and evaluation of the BEC's activities to gauge the effectiveness of its accomplishments.

² Industry Commission. 1996, page 87.

Audit Steering Committee

In line with the Audit Office's established practice for the conduct of performance audits, a steering committee was convened to reflect stakeholder views. The committee provided input to the audit's methodology and reviewed the draft report upon its completion. The Auditor-General chaired the steering committee and its members were drawn from the following areas:

- ?? Department of Premier and Cabinet;
- ?? Department of State Development;
- ?? Tasmanian Chamber of Commerce and Industry;
- ?? School of Government - University of Tasmania; and
- ?? Representatives of the performance audit section.

Audit Methodology

The following methods were used during the course of the audit to gather evidence from which conclusions were drawn:

- ?? Discussions with managers at DSD involved in assistance to industry as well as Business Enterprise Centres;
- ?? Review of documentation relating to individual assistance proposals, including: background research for assistance programs, applicable policies and procedures manuals, cost benefit analyses and business case strategy documents, correspondence relating to proposal and finalisation of the assistance package, contracts, and Board papers and minutes;
- ?? Discussions with facilitators from the three BECs visited; and
- ?? Annual reports, applications for assistance and performance management reports from the three BECs.

Audit Resources and Timing

Planning for the performance audit commenced in November 1999. Testing occurred in December 1999 through January 2000. The report was finalised in June 2000.

The total cost of the audit, including the cost of Tasmanian Audit Office staff, is estimated at \$61 000.

BACKGROUND

The role of the State in identifying and converting industry development opportunities into economic growth is a high-profile and sometimes controversial function, particularly as the levels of assistance across Australia are guarded routinely from public scrutiny under the shield of 'commercial-in-confidence'.

Governmental assistance to industry can take a variety of forms including:

- ?? Promoting export production relative to production for domestic sale;
- ?? Providing assistance based on certain industry characteristics, such as the exemption from payroll tax of businesses under a certain size;
- ?? Encouraging the development of a specific industry;
- ?? Regional assistance; and
- ?? Promoting individual firm or 'one-off' projects.³

In its 1996 report the Industry Commission recognised the difficulty of differentiating between the beneficial and harmful aspects of government assistance to industry. However, it did note that a distinctive feature was its discriminatory nature. The Commission's report identified the following consequence in relation to assistance:

'By providing assistance to some economic activities in preference to others, government action alters the incentives to participate in particular activities and can lead to a shift in the distribution of resources between activities.'⁴

This situation is exemplified by relief from or reimbursement of payroll taxation for a period of time as a component of assistance to selected companies. Assistance of this nature featured in several of the examples examined by the Audit Office. In connection with payroll taxation the Tasmanian Chamber of Commerce and Industry made the following point in its submission to the Industry Commission:

'A taxation holiday for the favoured enterprise or industry by definition means that the balance of industry is paying more taxation than it should. ... Put another way, if there is a capacity to reduce taxation, then the relief should be spread across the business community generally.'⁵

The Audit Office has no mandate to consider whether the State should continue to provide assistance to industry by this or other means as it is a matter of government policy. However, it would be advisable for that policy to be subject to high level economic analysis from time to time. Such analysis has not been carried out in Tasmania but the situation is not unique to Tasmania. The Industry Commission reported that:

'The Commission found very little evidence of systematic ex-post evaluation of assistance programs by States, including selective assistance programs.'⁶

Nonetheless, each State and Territory is active in providing assistance to industry. In Tasmania DSD is charged with the primary responsibility of improving the State's economic development. DSD came into being in September 1998 following a change of Government

³ Industry Commission. 1996, page 5.

⁴ Industry Commission. 1996, page 4

⁵ Industry Commission. 1996, page 49

⁶ Industry Commission. 1996, page 85.

and was formed by amalgamation of a number of other entities, including the Major Projects Team (MPT) and Tasmanian Development and Resources (TDR). In 1996 MPT had been separated from TDR and re-positioned in the Department of Premier and Cabinet (DPAC).

Under an initiative of the present Government an Industry Development Plan (IDP) was developed. Within the IDP the Department is viewed as a cornerstone, which: "identifies and converts all industry development opportunities into economic growth realities"⁷. The Audit Office supports DSD's initiative in developing a long-term strategy to determine the direction that the State's industry assistance program should take. This would provide a framework to guide economic growth and rationalise decisions as to which industry sectors should be supported or attracted through State assistance measures. Since this plan was released in 1999, however, those projects that were examined by the Audit Office pre-date it.

The employment situation in Tasmania has improved over the last four years, as can be seen from Table 1. Despite a small downturn in 1999 there has been an overall increase of approximately 4% between 1997 and March 2000. Part of this growth in jobs can be directly attributed to assistance to industry, particularly the establishment of call centres. DSD does not claim, however, that the overall improvement in the State's employment levels are attributable to the assistance to industry program alone.

| Year (At June) | Persons ('000) |
|----------------|----------------|
| 1997 | 191.6 |
| 1998 | 196.3 |
| 1999 | 195.9 |
| 2000 (Mar) | 199.2 |

Table 1: Total Employed Persons – Tasmania
(source: ABS)

The cost to Government of maintaining the industry development function is considerable. Table 2 details the associated expenses and revenues as advised in the Department's 1999 Annual Report.

| Item | Output Group: Industry Development | |
|-------------------------------|------------------------------------|---------------|
| | 1999* \$'000 | 1998* \$'000 |
| Administration expenses | 13 168 | 14 757 |
| Development expenses | 13 713 | 7 849 |
| Finance expenses | 8 462 | 10 833 |
| Total cost of services | 35 343 | 33 439 |
| Revenues | 7 283 | 13 390 |
| Rev. transfer to Treasury | (5 062) | (7 652) |
| Net Cost of Services | 33 122 | 27 701 |

*These activities have been funded by Treasury appropriations

Table 2: Expenses and Revenues – Industry Development
(source: DSD Annual Report 1998-99)

⁷ Industry Development Plan. 1999, page 1.

No statistics were published in DSD's Annual Report that would enable a determination of the efficiency (for example on a cost per job basis) with which the expenditure reported above has contributed towards attaining the desired employment objectives. However, during this reporting period DSD was going through a construction phase in which new assistance to industry programs were being developed in line with the Government's IDP. As explained in the DSD Annual Report, statistics were in the process of being developed.⁸

Most if not all of the examples of assistance tested by the Audit Office were made in the period prior to the existence of the IDP. Potential projects appear to have been assessed on a case-by-case basis, rather than having companies compete for the funding from a pool of resources. As a result, it appeared to lack a systematic, structured approach and tended to be driven by applicants rather than operating in response to a pre-determined policy that sought to steer State assistance in a particular direction.

The Industry Commission has also noted other issues that arise in relation to case-by-case assistance⁹. Firstly, public faith in the integrity of the political system can be undermined by perceptions of selective assistance while secondly; the case-by-case approach tends to attract larger firms that are better resourced to produce proposals.

Examination Focus and Approach

The Audit Office's work encompassed State assistance in the form of direct payments or indirect forms such as relief from payroll taxation or development of infrastructure. Amongst those cases reviewed were some new enterprises that were attracted to Tasmania by assistance, particularly call centres, as well as instances where assistance was made to facilitate the retention or expansion of existing businesses. Also included was a guarantee made by DSD to a company in the State's north-west. The selected assistance packages were reviewed using the audit criteria described in the previous section.

Included in the category of general assistance were a number of internal administrative payments that had been classified as 'assistance' in DSD's accounting system. Two cases initially included in testing were found to have been provided under the Commonwealth's 'AusIndustry' program and on that basis were beyond the scope of the audit. Details of cases reviewed in this audit are shown in Table 3.

| Type Reviewed | Subsequently Excluded | Number Selected |
|---------------------|-----------------------|-----------------|
| Guarantee | | 1 |
| General assistance* | | 13 |
| | AusIndustry (Cwlth)** | (2) |
| Call centres | | 5 |
| Total | | 17 |

* Includes 4 administration payments that were examined in the audit ** Outside scope of audit

Table 3: Cases Reviewed by Audit

⁸ DSD Annual Report. 1999, page 98.

⁹ Industry Commission. 1996, pages 47 – 49.

In addition, three Business Enterprise Centres funded through the Department's LEI Program were examined against DSD's guidelines relating to that program.

A list of the firms/projects reviewed during the audit is given in the Appendix.

Reviews and Audits in other Jurisdictions

A number of reviews on the topic of industry assistance have been carried out by other Audit Offices in Australia:

- ?? In 1998 the Audit Office of New South Wales issued a report titled *Department of State and Regional Development: Provision of Industry Assistance*. The audit had the objectives of assessing the adequacy of processes which underpin the provision of industry development incentives and evaluating the effectiveness of the management and administration of industry development incentives.
- ?? In October 1995 the Victorian Audit Office issued its Special Report No 37 titled *Promoting Industry Development: Assistance by Government*. The overall aim of the audit was to assess the extent to which strategic and operational policies in place within the Department responsible for assistance to industry were conducive to achieving maximum effectiveness in program delivery and performance.
- ?? The Western Australian Office of the Auditor-General released a report in 1994 titled *Financial Assistance to Industry*. The objective of the audit was to assess the effectiveness of the administration of such assistance. The scope included an examination of financial assistance legislation, promotion of financial assistance, assessment and approval of applications, monitoring, reporting and evaluation of program effectiveness and loan and investment recovery and write-off.
- ?? The Queensland Audit Office carried out a review in 1995 on the Industry Location Scheme, which encouraged businesses to locate its premises in that State. Objectives of the audit were to ascertain whether the Scheme's objectives were clearly defined and consistent with legislative and other requirements, and to assess the adequacy of the management systems within the Scheme.

FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

Call Centres

Call centres are facilities where groups of people handle large volumes of incoming or outgoing phone calls for the purpose of sales, marketing, customer service, technical support or other specialised business activity. They are typically set up as a large room with workstations that include a computer, a voice terminal connected to an automatic call distributor, and one or more supervisor stations. Each call centre may stand alone or be linked with other centres.¹⁰

Call centres have become a feature of Tasmanian economic life presently accounting for approximately 2 500 jobs. In addition to the jobs they have brought they also provide an opportunity for the State to move into the expanding area of customer-focused, technologically-based tertiary industry. Such enterprises are of interest to other States and there is intense competition to secure these projects. While a range of factors influence companies' decisions about location (eg comparative property costs, telecommunications costs, availability of skilled labour), Government assistance appears to be a necessary ingredient. Inducing companies to establish their operations in one State rather than another requires a balanced approach that on the one hand incorporates a sophisticated strategy to attract business but on the other a clear understanding of the benefit and cost implications that apply to the attraction package offered.

The audit methodology applied in relation to assistance to industry was derived in part from a report published by the Audit Office of New South Wales (*Department of State and Regional Development: Provision of Industry Assistance*) in December 1998.

Four different stages were examined in relation to the test sample, namely:

| | |
|------------------|--|
| ?? Pre-proposal | Comprehensive information on the Tasmanian economy is readily available; relevance of information for determining eligibility for assistance; |
| ?? Assessment | Guidelines in place to determine appropriate and consistent levels of assistance; |
| ?? Negotiation | Roles and responsibilities of parties involved in negotiation are clearly understood. Mechanisms in place to ensure that offers do not exceed permissible level; |
| ?? Post-Awarding | Adequate performance evaluation processes and procedures applied. Performance indicators exist to encourage maximisation of net economic benefits. Inclusion of clawback conditions where terms of assistance not met. |

The Audit Office reviewed the DSD processes that surrounded the successful establishment of five call centres in Tasmania. Information was gathered through discussion with departmental staff and examination of files and policy documents. Within each of the foregoing stages a number of questions were framed around salient control points.

¹⁰ Lucent Technologies/CRM Institute. 1999. 'What is a Call Center?' <<http://www.lucent.com/enterprise/ci/barney/callintro.html>> (29 February 2000).

Pre-Proposal Stage

DSD's approach in relation to seeking call centre operators is to aim for the 'blue chip' market segment. The decision was made not to target telemarketing and predictive-dialling call centres as these, although creating employment, sometimes have a poor reputation with regard to working conditions or career prospects. Instead, the Department attracts major businesses prepared to make long-term commitments and whose presence would signal to other companies that Tasmania is the best location for this kind of business activity. As with general assistance, a case-by-case approach is used to select and assess proponents on an emergent basis. This has the implication that proponents are not required to compete for a limited pool of assistance resources. This absence of a competitive process can have the effect of reducing the negotiating leverage which DSD could otherwise have, while increasing the negotiating power of a proponent which is able to identify several competing locations for its investment¹¹.

Staff in the Investment, Trade and Development Division (ITD) of DSD are pro-active and identify call centre opportunities by contact with companies, use of industry knowledge and information gained through research. DSD appoints a project manager to deal directly with the investor and to act as a link to other government agencies, both State and Federal. Thus the manner in which the proposal comes about in regard to call centres is from the Department rather than from the company.

One of the fundamental questions of the pre-proposal stage was whether the level of assistance offered was consistent with the expected benefits. Broad parameters for the financial incentives that are discussed in the pre-proposal stage are contained in the Call Centre Investment Attraction Strategy (CCIAS) approved by the TDR Board in December 1998. Rather than adopting a set 'checklist' approach to deriving assistance packages, the components that comprise a particular package are flexible and can be varied according to circumstances. Reasons for this adaptability are due to variations in businesses' perceived relative importance of the factors on which their location decisions are made, attitudes to and expectations of receiving assistance and profile of the target organisation. In the past, the components of assistance packages have encompassed grants to subsidise rents, recruitment or training costs, reimbursement of payroll tax payments, infrastructure, relocation costs for equipment or staff or in-kind facilitation assistance.

In view of the complexity inherent in assistance, for packages that have to be tailored to meet specific needs, the CCIAS specifies a benchmark expressed in terms of cost per job, with an upper limit prescribed. Consequently, DSD's methodology is determined by dictates of the market rather than being based on an economic analysis of how to maximise returns on funds expended. The Board paper that approved the CCIAS stipulated that future presentations to the Board about new or expanded call centres contain tables detailing levels of current and projected employment, Government funding and actual net present value (NPV) cost per job compared to the benchmark NPV cost. The Audit Office noted that submissions made to the Board did not seem to contain an analysis of potential risks or exposures associated with the proposal.

NPV is a single figure that represents the equivalent of a stream of future net cash flows over a period of five years. These cash flows are all converted to present-day values using a discount rate. To arrive at the cost per job the NPV figure is divided by the number of jobs created in the project being assisted. This figure is a once-only, up-front cost and not an ongoing outlay. The benchmark figure has been derived on the basis of what the market

¹¹ AONSW. 1998. Department of State and Regional Development – Provision of Industry Assistance. Sydney: Government Printer, page 25.

apparently requires in order to compete with offers being made by other States. The cost-per-job methodology is useful for comparative purposes or as a practical measure in those cases where localised employment is the major concern and where the scale of assistance is not large.

For major projects, say those involving over a million dollars of assistance, it should not be considered an appropriate substitute for cost-benefit analysis. Such cases require more sophisticated economic modelling that would examine the broader effects on the State such as calculation of real per capita Gross State Resident Product, the effect on the state population, state employment and cost benefit analysis¹². That broader analysis should examine the alternative use of funds in a standard base case. It is significant that there is currently no reference to, or calculation of, the economic benefits to the State. Indeed, the Industry Commission stated that during its inquiry into government assistance to industry it was not made aware of any attempts to identify or measure the 'optimal level' of assistance to be generated or how to identify the key drivers.¹³ As well, the Audit Office of NSW considered that the NSW Department of State and Regional Development's assessment methodology needed to examine more fully the entire direct and indirect costs and consequences of assistance proposals.¹⁴

A section of the CCIAS deals with the method to be used in calculating the cost per job. It states that all assistance and subsidies from the Government should be included, however there are exceptions. Firstly, in call centre cost-per-job calculations DSD does not take payroll tax rebates into consideration. The rationale for its exclusion is given in the CCIAS, paragraph 8.3 which states:

' ... the stream of payroll tax revenue that would not have otherwise been received by the Government without the assistance package will be ongoing for the life of the call centre.'

This justification obviously depends on the assumption that the attracted business will not relocate to another State, cease operations or require additional assistance at the end of the 'tax holiday'. The justification also requires that any payroll tax implications are considered in alternative competing uses of the funds.

The Department considered that foregoing this form of revenue was a necessary part of a longer-term strategy of investment attraction and job creation. From the Department's viewpoint, relief from payroll tax was another element that could be used to develop flexible assistance packages that reflect an applicant's requirements or expectations. There was scope to vary the period of tax relief and from the sample examined by the Audit Office three years per developmental stage appeared to be usual although one case was noted where the duration was four years. Payroll tax relief was capped in terms of specified numbers of positions created and was subject to clawback provisions if targeted levels of employment were not achieved.

A consequence of this policy in relation to the treatment of foregone payroll tax is that centralised records are not kept. This is apparently the case in other jurisdictions as well. The Industry Commission noted that it: 'had great difficulty gathering information on the

¹² Based on some economic modelling, the Industry Commission found that: "Most States do gain slightly in terms of per capita GSRP ... however, this projected effect seems to come primarily from a projected lowering of the population ..." (Industry Commission. 1996, page 579.

¹³ Industry Commission. 1996, page 34.

¹⁴ AONSW. 1998, page 48.

extent of State ... government revenues foregone, particularly exemptions and/or rebates relating to individual companies or projects.¹⁵

The other exception in cost per job calculations concerns the capital cost of the first of the call centres established. It was explained by DSD that this expenditure was a strategic investment that was aimed at attracting future investors to the State. This decision may have been vindicated by subsequent growth of call centre activity in Tasmania but DSD has left the way open to pursue this path again, as stated in the CCIAS, paragraph 8.0:

'Whilst the building of call centres by the Government is not the preferred method of procurement, circumstances at the time may dictate that it is necessary in order to secure a new call centre operator in the State.'

The Audit Office considers that a more holistic evaluation of a project, which takes into account all of the costs involved in direct assistance, would assist in decision-making in regard to the allocation of limited resources.

As part of the pre-proposal stage, publicity material promoting the State as the ideal call centre site was examined during the audit. The presentation style adopted conformed with that already used by Tourism Tasmania where the State's logo is incorporated as a distinctive branding feature. To prolong the shelf life of printed materials (and thereby maximise cost effectiveness) texts avoided the use of date-related information. The Call Centre brochure, which was part of a larger, more comprehensive and impressive kit, explained how government support could assist new businesses with start-up packages. The brochure also contained colour leaflets from two of the national companies operating Tasmanian call centres in which the CEOs endorsed Tasmania as a base for these activities.

Recommendation

In addition to the cost per job benchmark DSD should consider using a basis of evaluation of major projects for assistance (e.g. where the aid will exceed \$1M) that includes analysis of benefits to the State, as well as reflecting all related costs.

Assessment Stage

The second stage of audit testing reviewed the level of documentation of assessment mechanisms in order to ascertain the degree of standardisation of procedures. Testing also sought to verify that all proposals were treated equitably and that DSD had documented assessment mechanisms that were consistent with the competitive neutrality principles of the NCP. Two issues were of particular concern here: firstly, that in the interests of equity public funds should not be used to advantage one enterprise over another. Secondly, to ensure that existing businesses are not harmed by State assistance to another in that industry sector.

The CCIAS referred to above is the control against which assistance packages are assessed. Vetting and approval by the Board was a regular feature of the assistance packages reviewed. Segregation of duty was also noted and the assessment process routinely involved more than one officer.

Each of the call centre proposals examined by the Audit Office fell well within the parameters of the CCIAS in regard to the cost per job benchmark.

So far as the equitable treatment of proposals was concerned, call centre projects have occurred individually and been treated accordingly. Therefore the situation had not arisen

¹⁵ Industry Commission. 1996, page 14.

where applicants were competing with one another for a limited resource and DSD has not had to consider the potential adverse impact on other competitors or operators. None of the proposals in the sample appeared to have any potential to impact adversely on other businesses in the sector.

Another element of the assessment stage involves consideration of local employment factors. In this process DSD weighs siting options for new developments against employment opportunities in competing localities.

Negotiation Stage

Although the final outcome of discussions between proponents and DSD was evident from papers examined – and in line with the CCIAS – the details of negotiations were not sighted. From discussions with Departmental officers the Audit Office was satisfied that the responsibilities and accountabilities of DSD staff involved in negotiations with proponents are clearly defined and understood. Nonetheless, this lack of transparency meant that it was not possible to confirm that the assistance package finally agreed was at the minimum level even though it may well have been. There was a further condition that funds would not be advanced by DSD until formal documentation was in place to the satisfaction of the CEO.

Assistance was provided on the basis of formal performance agreements which targeted pre-determined employment levels. Claw-back provisions were incorporated in the grant deeds for all packages reviewed, requiring proportional repayment to the State if required levels of employment or investment were not achieved. It was considered that such clauses were comprehensive and clearly-worded, similar to the rest of the agreements sighted and the contracts were drafted by commercial law specialists.

In a number of instances call centres are built on Crown land, in which case the State becomes the lessor. The Audit Office understands that while the Department attempts to minimise situations where this is the case, it can become a commercial enterprise of last resort. Where this has occurred DSD has adopted a staged approach. In the transitional phase the government accepts the risk on the development proposal and subsequently transfers the risk, which is substantially reduced, to a private sector third party.

During the course of the audit it was apparent that grant files did not always contain the necessary documentation to obtain a complete picture of the assistance process. This was especially notable in the negotiation stage. DSD's explanation was that this stage was regarded as particularly sensitive and that commercial-in-confidence considerations led to a reluctance to document the process.

Post Awarding Stage

Following the contract finalisation, documentation relating to monitoring was noted in regard to updates in the Board minutes and papers. In addition, as a check on the anticipated number of new jobs, statutory declarations were sighted in support of claims by the companies for refunds of payroll tax, training or other costs, etc, commensurate with the terms of the grant deed. The risk of mis-reporting employment levels in order to fraudulently maximise tax concessions is minimised due to the penalties that apply to perjury under Tasmania's *Evidence Act 1910* if a statutory declaration is false.

In regard to post-assistance evaluations, it was noted from discussions with the officer in charge of call centres that his section carries out 'big picture' analyses (on which types of call centre companies to focus on), and how to improve contractual arrangements, negotiation processes, and marketing methodologies. It is considered that such an approach enables organisational learning to occur and thus improved effectiveness of future negotiations, contractual provisions and management of the client.

Striking a balance between maintaining transparency of reporting to the public with the need for commercial confidentiality is a sensitive issue in relation to Government assistance to industry. This is especially so in the case of call centres where States are vying with each other to gain new businesses.

Agreements made in respect of call centres were examined and indicated that there were adequate provisions to ensure that commercial-in-confidence issues can be balanced with public reporting requirements.

Conclusion

Although it was possible to construct an audit trail, except for the negotiation stage, the Audit Office believes that transparency could be improved. By keeping all relevant papers, including notes on monitoring and on-site visits, on a client file it would be much simpler to review individual examples of assistance.

In regard to the Department's strategy for development of call centres it is considered that industry assistance is administered in a satisfactory manner, with the exception of the existence of a comprehensive tool for evaluating assistance for proposed projects.

Assistance to Industry – General

In reviewing DSD's approach to the administration of assistance the Audit Office sought information on guidelines or manuals available to staff. There was a *Finance Division Policy and Procedures Manual* that was issued in 1992 dealing mainly with loans. Although it had not been updated recently, it is still applicable as it addresses issues such as assessing the competitiveness of a client's prices, adequacy and currency of stock-on-hand, etc.

As a general guide DSD also uses the *Best Practice Guide for the Administration of Grants in the Tasmanian Public Sector* circulated by the Department of Treasury and Finance (Treasury) in 1996 and based in turn on a similar publication of the Australian National Audit Office for use in the Australian Public Service. Although the Treasury guide was not intended to take the place of agencies' own guidelines no more recent or specific guidelines have been produced by the Department.

In response to an Audit Office query on the seeming lack of current documented procedures DSD explained that whilst the Department was conscious of budget appropriation issues, the need to retain flexibility in the face of intense competition from other States was paramount. It was stated that guidelines, by their very nature, could be restrictive and limit the ability of DSD staff to tailor packages to potential investors. As well, it was pointed out that packaging financial assistance to a level that is not necessarily required could have adverse budgetary impacts. Control of the process is maintained by means of segregation of duties combined with a fixed structure of approval levels involving DSD's Board.

Although the Audit Office accepts that restrictive guidelines are not desirable, documentation of procedures does need to be available as a reference for staff and to clearly articulate the objectives of processes. In the absence of such material, roles and responsibilities are not clear and control weaknesses can evolve.

Analysis of potential risks and exposures for the Department in connection with general assistance packages did not seem to be part of submissions presented to the Board. To assist in decision-making processes and to ensure a standardised approach, the Board paper template should include a section dealing with the potential risks and exposures relating to proposed project assistance

Recommendations

DSD should produce its own departmental guidelines on the administration of assistance.

The Board paper template should include a section dealing with the potential risks and exposures relating to proposed project assistance.

The test sample was selected on a judgement basis to include a variety of industry sectors and a variety of commercial operations ranging from fledgling businesses through to global enterprises. The sample included some projects that had been handled by the former MPT. It was noted that the files did not always contain enough information to adequately convey the rationale for decisions made in relation to assistance. As a result a clear audit trail could not be followed in respect of the examples of assistance reviewed.

Pre-proposal Stage

Many of the assistance packages now in DSD's portfolio were previously part of DPAC's MPT program. Some had arisen primarily from Ministerial consideration of local employment issues such as imminent factory closures or scaling back of operations. As such they were not part of an integrated program but instead appeared to have been developed on an *ad*

hoc basis rather than following a strategic method of planned assistance to particular industry sectors.

In regard to earlier programs operated by DSD, assistance was provided to primary industry under the auspices of the previous Rural Adjustment Scheme (now replaced by FarmBi\$) and training assistance. Currently, the emphasis of these activities is on lending with a focus on the overall business. ITD, however, focuses on improving particular aspects of a business.

Samples of DSD's publicity materials were reviewed during the audit. Senior managers within ITD oversee the design and production of brochures and other materials to ensure that targeted groups would find them easy to understand. New stocks were commissioned late last year with a design that incorporates the State's logo, familiar through Tourism Tasmania campaigns, as a well known and distinctive brand identifier. The quality of the printed media appeared to be commensurate with the image that was being projected. Care was taken with the use of text in printed items to avoid the use of titles or names that could change in the short term and restrict their shelf life.

Publicity materials were often formatted as folders or covers into which other papers could be inserted thereby promoting a particular company or feature of Tasmania.

Assessment Stage

Competitive neutrality is a principle of the NCP that has two main thrusts. Firstly, on equity grounds, public funds should not be used to favour one business over another. DSD takes account of structural adjustments occurring within industry sectors and looks at wind-down arrangements.

Secondly, assistance to individual companies may direct activity away from enterprises engaged in that same activity in another State thus hampering national microeconomic reform. DSD's State Industries Division has a number of programs that target industry sectors. However, proposals that come before ITD are usually handled on a case-by-case basis. Nonetheless, and in keeping with the NCP principles referred to above, there is an emphasis on assisting industries rather than favouring individual businesses and the packages put together in respect of call centres, aquaculture and textile manufacturers reflect this.

Substantial credit checking and due diligence as to the viability of an organisation's proposal are carried out in the assessment stages. DSD's librarian is the only officer authorised to obtain credit histories because of sensitivity to privacy concerns. An extensive library has been compiled in this regard by the Department.

Discussions with the proponent are used to determine feasible targets in terms of the level of assistance being offered. DSD's internal review processes ensure that adequate and measurable indicators are included in agreements as are clawback provisions in the case of goals not being achieved. Key performance indicators that have to be satisfied in any grant support situation include, but are not limited to, number of jobs created or secured, investment created, new markets established and new contracts negotiated.

Due to the variable nature of industries and proponents, there are no hard and fast guidelines in respect of due dates for the Department to prepare proposals. The ethos of DSD is such that assessments are treated expeditiously although delays can occur from the proponent's side, particularly after a proposal has been made. This situation can introduce a great deal of uncontrollability in finalising assistance as was evidenced in some cases reviewed by the Audit Office.

Internal review processes and Board approval provide a means of ensuring that assessment mechanisms are consistently applied. However, written records relating to the assessment stage were frequently not available. Board papers were examined during the audit but it was found that supporting documentation on some of the files relating to assistance was incomplete. When these cases were followed up with DSD additional documents were usually obtained from other files or sources. This incomplete audit trail on assistance files reduced the level of transparency making it difficult to understand the decision making process.

Preference is given to types of assistance with the lowest risk exposure to DSD while meeting the client's funding needs at the same time. Specific ceilings are not used for other types of assistance but the limit applied for call centres is used as a benchmark for consideration of cost per job created or retained. The length of the contract period is also examined for reasonableness.

Recommendation

Assistance to industry files should contain complete documentation to allow straightforward examination of projects and to ensure transparency of management processes.

DSD Comment

It is DSD's view that grant file documentation should focus on outcomes and not detailed, over-bureaucratic information regarding process.

DSD has now updated and implemented its Project Client Management System (PCMS) to record the majority of process information to ensure transparency in this area.

Negotiation Stage

There are two possible methods of arriving at this stage. Applicants can either have responded to the State's marketing strategies (as described in the Pre-proposal Stage) or they may have been contacted directly by staff of ITD.

At the negotiation stage the State's proposal to attract industry is considered and the applicant responds to it. General Managers of ITD control assistance packages in a project team environment that ensures a standardised methodology and a segregation of duties. Negotiations are usually conducted by the two most senior managers of ITD who appreciate the need to include in agreements attainable and measurable PIs as well as clawback clauses. A review process forms part of DSD's internal controls and draft agreements are vetted before being presented to applicants.

The existence of an audit trail is essential at this stage to ensure that transparency and probity issues are addressed. While DSD has a computerised client management system (PCMS) that officers use to record details of meetings, phone calls, interviews, E-mails etc with respective clients it is not yet fully implemented and is not used for note-taking during the negotiation stage. It is understood that when fully implemented this system will have the ability to furnish an audit trail of not just the negotiation stage but the entire grant administration process. The Audit Office could only find evidence of negotiation documentation relating to one of the cases reviewed. However, when asked for comments on this matter we were told that documentation on the negotiation phase is rare due to concerns about maintaining confidentiality during this crucial stage. Accordingly, the Audit Office considers that with such an attitude against documenting this kind of activity, the likelihood of future use of the corresponding fields in the Department's PCMS is low. A need for confidentiality during the negotiation stage does not imply a need for confidentiality of the outcome.

Recommendation

The issue of commercial confidentiality should not take precedence over governmental accountability and DSD should document the rationale for all decisions made during the negotiation stage.

DSD Comment

DSD officers are trained to document outcomes of negotiations.

Negotiation strategies are developed in advance of negotiations for every project through the project approvals process by the Board or Executive.

To document every negotiation point or indeed, the rationale for decisions, is far too bureaucratic.

Under the broad heading of "Options for Improving Performance" the Industry Commission has considered a range of enhanced reporting procedures. Items that are discussed in this context in the Commission's report include:

- ?? Criteria and approval procedures used to assess assistance provided; and
- ?? A demonstration that anticipated benefits would outweigh the costs.

Additionally, the Industry Commission was of the opinion that there should be public disclosure regarding assistance to individual firms or projects. Amongst other things this level of disclosure should include:

- ?? Duration of assistance; and
- ?? Estimated value of concessions (tax, land or government charges).¹⁶

In the case of revenues foregone the recommendation is made that State revenue or taxing authorities should estimate and publicly report the cost of such exemptions.

In making these disclosures there is no suggestion that any details of the applicant's financial position or commercial processes would be included as they are properly confidential between the parties.

The Audit Office agrees with the policy of public disclosure of the estimated value of assistance provided on a project by project basis. It is acknowledged, however, that public disclosure is a sensitive issue and the Industry Commission has noted significant variability both between and even within States. Although the fact that States are involved in stand-alone zero sum negotiations has been used to justify continued secrecy it represents another cost to society arising from bidding wars, namely the undermining of good government.¹⁷

There is an additional benefit that could attach to disclosure regarding the duration of assistance. Employees, investors and the public at large would be reassured to know that relatively "footloose" industries (as is the case with call centres) have made a binding commitment to the State for a specified time period.

In balancing considerations of commercial confidentiality with the public's right to know, DSD already informs proponents that as grant funds are sourced from public moneys it reserves the right to make general disclosures regarding the assistance given. This condition is explicit in agreement documents.

¹⁶ Industry Commission. 1996, pages 83 - 85

¹⁷ Industry Commission. 1996, page 82.

As to the objective of seeking to balance the appropriate amount of assistance with the projected benefits to the State, research and discussions held with clients in the early stages ensure that officers gain an understanding of the type and level of assistance most needed. This understanding of what the applicant actually needs is then aligned to the range of the Department's assistance options to produce a firm proposal of what the State is likely to offer and what the corresponding benefits will be. A paper is then prepared for the Board in which a recommendation for a particular course of action is made.

After due consideration and ratification by DSD's Board the *Tasmanian Development Act 1983* requires that ministerial approval be obtained for all grants up to \$100 000 with further approval from the Treasurer necessary for those grants exceeding \$100 000. After such approval by the Board, and if applicable the Treasurer, is obtained the proposal is forwarded to the responsible minister for final approval. It has been usual practice over a number of years for the Premier also to be responsible for the portfolio of State Development. In the sample examined during the audit no instance was noted of a Board recommendation being rejected by the minister or conversely of the minister approving a grant that had not been recommended by the Board.

Recommendation

There should be public disclosure regarding firms or projects receiving government assistance and details of benefits provided.

DSD Comment

It is DSD's view that public disclosure of sensitive private sector information would be detrimental to DSD in its dealings with private sector organisations.

Enterprises are extremely sensitive about information they provide to government, as it usually contains their key future financial and business planning strategies.

Disclosure of information would obviously be of advantage to competitors within the industry. Disclosure would cause the enterprise seeking assistance to have less confidence in government and they would probably seek alternative assistance from providers that would guarantee security of information provided.

Alternatively, if government sought less information from enterprises, it would compromise DSD's current assessment process.

Post-Awarding Stage

Performance measures evolve from the previous stages where the particulars of assistance are discussed and refined. Through ascertaining which targets (eg export earnings, jobs created or secured) are attainable meaningful performance indicators (PIs) are derived. The objectives of the post-awarding stage are to ensure that monitoring processes are closely tied to the targets expressed and commensurate with the degree of risk to public funds. DSD has a section that manages loans and grant deeds to ensure that targets and milestones are achieved.

Detailed financial analysis of businesses assisted, such as reviewing quarterly statements, is not an automatic part of this stage but may be included if it is written into the conditions of the grant deed. Where assistance was tied to certain numbers of jobs created or retained, relief (by way of reimbursement) from payroll tax was sometimes a part of the package. In some of these cases, reimbursements were based on supporting financial records such as payroll numbers and corresponding sums paid to State Revenue. More often, however, reliance was based on statutory declarations made by the chief finance officer or some

equivalent senior officer of the client organisation. This form of reporting is viewed as reliable as was explained above in relation to call centres.

Monitoring was more likely to take the form of on-site visits and inspections which had the advantage of maintaining closer contact with the business and therefore permitting an opportunity of gaining information directly. Although it was ascertained that follow up reports on the grantees reviewed by the Audit Office had been presented to the Board it was noted that these papers were often not held on the assistance files which made review of management processes difficult to confirm.

In ITD officers who deal with clients are aligned with industry sectors to ensure an ongoing relationship with that industry. Further, as conditions of granting aid routinely require ongoing contact between DSD and clients over a period of years, considerable feedback on the assistance process, from the point of view of both the Department and the recipient, is available. The corporate planning process is linked to monitoring of past performance. For example, in 1999 the Premier required each Departmental area (including State Industries and ITD) to report three major successes in the past year and three planned for the following year.

Conclusion

It is considered that the Department's management of this area is satisfactory in regard to the pre-proposal and post-awarding stages. However, difficulties were encountered in following an audit trail during the assessment stage. In regard to the negotiation stage of assistance improved transparency could be achieved through more complete documentation. We consider that there should be greater public disclosure of the assistance provided in the post-awarding stage.

Guarantees

During the audit a Government guarantee extended by DSD on behalf of a textile company that currently employs more than 270 people was examined. Guarantees are not the preferred form of assistance and in this case the guarantee was just one element in ongoing aid that had evolved and extended over a twelve-year period.

This particular case was an *ad hoc* arrangement that had arisen in part through ministerial concerns over job losses due to possible closure of the facility. Briefly, the earliest forms of assistance had included loans that were converted to equity (\$2M in preference shares) in 1994. Subsequently, the State purchased the site for \$7.8 million and offered rental at reduced rates.

In order to help the company onto a more secure footing and to safeguard the funds already invested in the business DSD provided a \$1M Government guarantee secured by a second debenture mortgage. The purpose of the guarantee was to secure alternative banking arrangements including a \$3M banking facility. To further strengthen its financial position a second guarantee of \$2.5M had been authorised but was not taken up at the time of the audit. DSD's efforts with this company have centred on strengthening its future prospects through increased productivity. Recent investments have ensured that the company has been able to remain competitive.

To date, the State has invested almost \$10 million in this business and as the relevant Board paper acknowledges 'the direct return on this investment has been very poor'. Although a financial analysis of the enterprise indicated that in the event of the business failing the State's investment in the business could be recovered the opportunity cost of the capital tied up in the business represents a considerable loss. On a cost-per-job basis the unaccounted for opportunity cost would greatly exceed the benchmark for other assistance to industry.

DSD Comment

DSD's support in this venture has been vindicated as the company is now growing, jobs in the region are secure, the company is increasing investment and an exit strategy for government equity funds has now been put in place.

Business Enterprise Centres

Business Enterprise Centres (BECs) are one element of DSD's business and economic support programs referred to as Local Employment Initiatives (LEI). The LEI Program was initiated in 1990 and aims to improve employment prospects through a partnership of the State Government and local communities. The underlying philosophy is a "bottom up" approach where organisations that are locally led and controlled respond to conditions and circumstances in their areas and develop strategies to foster business and job growth. Amongst other things these activities could encompass the consolidation of the local industry base, encouraging the retention of existing businesses and marketing or promotion of the area.

With a community-based focus BECs can better assist people who may be uncomfortable in dealing directly with Government agencies or who prefer a less formal approach, more akin to that of counsellor rather than adviser. Under the Department's guidelines funding is available for submissions made by BECs, subject to a review of previous performance, at a level of up to \$40 000 per year providing there is at least a matching contribution from the local community. These other funding sources include local businesses and Councils as well as revenue raised directly by BECs from fee-for-service activities.

A review of previous examinations of the LEI program was also a part of Audit Office activity in relation to the BECs. Consultants carried out a review in May 1996 and also found that the facilitator was a key determinant in a Centre's effectiveness. Amongst recommendations made in the report were more active participation by Boards, the use of strategic plans as a means of keeping a sharp organisational focus, improved statistical reporting (including simple client satisfaction surveys) and finally, that the role of DSD in relation to BECs should be to lead and energise rather than control.

Three BECs (Southern, Derwent Valley and Business East) were selected for review. The longest running of these is the Derwent Valley BEC (originally called "New Norfolk") which was established in 1990 as one of six pilot LEIs. Southern was originally the Glenorchy BEC and opened in 1993, but in 1996 it expanded its area of operations to include Brighton from which time the Centre became known as Southern BEC. Business East is the most recently established BEC and started operating in 1998. Audit Office testing encompassed five facets of BECs' operations, namely strategic planning, consistency with DSD's LEI program guidelines, assessment of performance, discussions with facilitators and finally a review of any previous examinations made of the program.

In reviewing the adequacy of BECs' strategic planning it was evident that although each one met DSD's guidelines the quality was variable. This was particularly evident so far as the focus was concerned. One of the BECs was extremely focused due to the linking between each objective and research undertaken in identifying needs and clear directions for maximising success. However, the plan of another BEC had a considerably narrower scope. For example, the mission statement of one Centre was seen to be more focused on the BEC itself, rather than how it could achieve an improvement to the local economy.

Another aspect of strategic planning examined by the Audit Office was the 1999 annual plan prepared by each BEC. DSD guidelines require that the following be provided:

- ?? Description of business assistance given;
- ?? A report by the Board;
- ?? Evidence of the BEC's contribution to economic development in the area; and
- ?? Audited financial statements together with an acquittal of DSD funding.

A review of the annual reports for each of the BECs indicated that these requirements had been met.

Consistency with DSD program guidelines was firstly examined in regard to BEC governance structures. It was found that each BEC had a legally incorporated Board with members drawn from a diverse range of backgrounds as required by the guidelines.

The second element of consistency with DSD program guidelines involved reviewing the role of each BEC facilitator, who is the person primarily responsible for his or her Centre. Due to the wide-ranging role of the position, the facilitator's approach is considered by DSD to be a key factor for a Centre to achieve success. One of the BEC's strategic plans described the facilitator's role and it was considered that the interpretation was consistent with the guidelines. While another of the BEC's plans had not included a position description, during discussions with the facilitator it was apparent that his role was consistent with DSD guidelines. The third BEC plan also had no description of the facilitator's role and the assessment had to be based on a skills inventory and a listing of the objectives for the Centre contained within the plan. From these sources it appeared that the main objectives of DSD's guidelines were met with the others noted in varying degrees.

The final element of consistency with program guidelines related to regular reporting by the facilitator to the BEC Board, as this is an essential element of corporate governance. Management reports prepared for the respective Boards were examined as were annual reports; both frequency and contents of the reports was found to be satisfactory, but different facilitators included varying levels of detail. Only one BEC included performance reports that were clearly linked to the strategic plan.

Assessment of performance, the third facet of BEC operations reviewed by the Audit Office, involved determining the degree to which BECs analyse data that they collect and incorporate the results into future targets and strategies. At one BEC the facilitator completed returns for DSD but thought that the information did not convey a complete picture of activities. Although this may be the case this particular Centre was also considered to lack an outward-looking focus on performance and strategy. The facilitator at the second BEC did not appear to use performance indicators (PIs) in a structured way in day-to day work, which may have been attributable to relatively lower levels of computerisation as well as the wider role that the Centre had within the local community. A more integrated approach typified the third BEC where PIs closely related to objectives listed in the strategic plan, as noted above.

It was of interest to note that one facilitator considered that a key statistic he worked with, persons agreeing not to proceed with a venture after seeking advice, should also be included in the quarterly data collected by DSD. This was based on the view that the impact of (yet) another business going into liquidation would be considerable on the local community. Cases of this kind were not uncommon and could involve considerable effort by the facilitator. In this regard, it was considered that the current quarterly performance indicators collected from BECs (businesses created/saved, jobs created as shown in Table 1) may not be adequate in obtaining a complete performance snapshot. As well, there is no recognition of jobs lost within the BEC's area of operations that would be useful in obtaining a balanced view of the overall level of performance.

Additionally, there has been the possibility that the above statistics could be double counted through inclusion in DSD's own records. Such a situation could occur where a person initially approached DSD directly, was referred to a BEC and then went on to start a business. This appeared to be due to a lack of precision in the LEI program guidelines covering the compilation of statistics.

Initiatives taken by facilitators to aid in job creation varied and necessarily reflected local conditions. Techniques mentioned by facilitators were assisting businesses in recruitment and selection processes, provision of information on budgeting and licensing, support with office and administrative services, space to set up a business and assisting with applications under the Commonwealth's NEIS funding.

| Entity | New Businesses Started | | Existing Businesses Saved | | New Jobs Created | |
|--------------------|------------------------|--------|---------------------------|--------|------------------|--------|
| | Target | Actual | Target | Actual | Target | Actual |
| Derwent Valley BEC | 16 | 11 | 2 | 1 | 24 | 19 |
| Southern BEC | 80 | 10 | Not Stated | 0 | 100 | 34 |
| Business East BEC | No Target | 9 | No Target | 6 | 80 | 68 |

Table 4: Selected 1998/99 Performance Measurements

(Source: DSD figures not verified by Tasmanian Audit Office)

Likewise, there are difficulties in assessing the effectiveness of other BEC objectives. Stated aims of the LEI program guidelines include increasing the level of profitable economic activity at the local level and encouraging the development of an entrepreneurial culture. While these are necessary elements to create and retain long term jobs in Tasmania appropriate and consistent performance indicators would be needed to evaluate them. The existing program guidelines do not stipulate these performance indicators.

So far as the relative success of each of the BEC's was concerned it was not possible to form an opinion. The setting of each Centre was inherently different, a factor that complicated measurement of the relative success of initiatives taken. The physical, economic and demographic features of the areas in which the three Centres operated varied so that strategies that worked in one location could not necessarily be applied in other situations.

To address this variety of settings and diverse skill sets of unemployed local people a range of strategies were applied by Centre facilitators. In keeping with the 'bottom-up' philosophy of the LEI program, facilitators typically sought to achieve job creation by establishing or strengthening networks with communities and business groups. For example, in one case a Vocational Education Committee was formed with funds being obtained under the Australian Student Traineeship Fund. Subsequently, traineeships were established that led to full time employment.

In gathering informal feedback from facilitators a number of observations were made. Perhaps the most striking impression gained from visiting the BECs was that the approach and focus of each Centre seemed to be strongly influenced by the personal style of the facilitator. Because of this, perceptions of success and desired outcomes are related to the individual's own views on the role of the Centre and its function within the local community. Audit findings were thus not made in respect of this aspect of BECs.

The first facilitator believed that he lacked support from DSD and it was noted in documentation reviewed that there was a reduction in community demand for the BEC's services. As this situation was not found in the other Centres sampled it might be that the decline was due to a mismatch between the approach of the BEC and the expectations of the community.

The second facilitator had a more community-focused view which was not necessarily limited to matters impacting directly on the local economy. This situation was partly decreed by the strings attached to funding that the BEC received from the municipal council. Consequently, the BEC was involved in assisting a sporting club and non-profit organisations. Similarly, job readiness for school leavers was another area of activity, even though it is not an explicit part of DSD's guidelines. It was also explained that the centre had embarked on a US-based community re-vitalisation program that should ultimately have a positive impact on the local economy. Based on outcomes achieved in the USA this program has the potential to address the LEI objectives of stimulating profitable economic activity and fostering entrepreneurial spirit in the area serviced by the BEC.

One of the BECs was quite different in its perspective, which again was a spin-off of the facilitator's personal style. A positive attitude was apparent and there was a readiness to try new approaches. Amongst these was the use of students (from both the local matriculation college who were studying business and Drysdale TAFE) who were used to undertake reviews and SWOT analyses. Stress was also laid on tapping into local community networks to create a widespread interest in local economic issues. So far as any overlap with DSD's responsibilities the view was held that this was something that could be used to the Centre's advantage.

This was in contrast to the other two BECs that had been established for a number of years and had received considerable funding under previous State and Commonwealth initiatives and were seen to be in the process of adapting to a regimen of restricted Governmental funding.

As can be seen from the above comments, each Centre had a different approach. One explanation is that DSD is just one of the sources of funding. With the balance of funding coming from their local community it is inevitable that Centres also have to reflect expectations and priorities of those communities. As a result, assessments of 'success' depend on which of the funding bodies' point of view is used. However, DSD could more clearly articulate its particular focus to the BECs and thus improve the alignment of the Centre's perspective with that of the Department. Accordingly, the LEI Program Guidelines must reflect DSD's current need for structured performance indicator reports.

Conclusion

Overall the Audit Office considered the LEI program to be running satisfactorily in regard to compliance with DSD's own Guidelines. Also, it is recognised that a degree of discretion is necessary for facilitators to manage their respective BECs due to the variety of economic, social and demographic factors that characterise the areas within which the Centres operate.

APPENDIX

Firms/Projects reviewed during the audit.

Ansett Australia Ltd

Australian Furniture Research and Design Institute Ltd

Australian Weaving Mills Pty Ltd

Comalco Aluminium (Bell Bay) Ltd

Copabay Pty Ltd [Pumphouse Point]

Cuthbertson Bros [Blundstone Pty Ltd]

Foley Industries Australia Pty Ltd [Tasman Hot Water]

Goldamere Pty Ltd [Savage River Mines]

Hokushin Co Ltd [Starwood Australia Pty Ltd]

Knight Bros Pty Ltd [Dorans Fine Food Pty Ltd]

Port Huon Industrial Site

Qantas Airways Ltd

Simplot (Aust) Pty Ltd Cold Stores

Southern Aluminium Pty Ltd

Taiwan Pulp and Paper Corporation

Tas Design Development Company

Vodafone Networks Pty Ltd

Watts Communications Ltd

Westpac Banking Corporation

Business Enterprise Centres reviewed during the audit.

Business East

Derwent Valley (formerly New Norfolk)

Southern (formerly Glenorchy)

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