HONG KONG APPLIED SCIENCE AND TECHNOLOGY RESEARCH INSTITUTE COMPANY LIMITED 香港廳用科技研究院有限公司



Your Ref.: CB(3)/PAC/R48

1 June, 2007

Clerk to Public Accounts Committee Legislative Council Legislative Council Building 8 Jackson Road Central, Hong Kong

(Attn: Ms Serena CHU)

Dear Ms CHU,

The Director of Audit's Report on the results of value for money audits (Report No. 48)

Chapter 2: Administration of Hong Kong Applied Science and Technology Research Institute Company Limited (ASTRI)

I refer to your letter of 29 May 2007 and attach herewith copies of the following minutes -

- (a) Minutes of the Special Review Committee held on 19 January 2007 Annex I;
- (b) Minutes of the Board meeting held on 20 March 2007 on the employment contract of Dr. Robert Yang Annex II;
- (c) Minutes of the Special Board meeting held on 27 February 2004 Annex III;
- (d) Minutes of the Board meeting held on 22 June, 18 September, 18 December 2006 and 20 March 2007 Annex IV;
- (e) Notes of the Special Meeting to review draft Audit Report held on 15 February 2007 Annex V; and
- (f) Minutes of the Special Board meeting held on 24 April 2007 Annex VI.



Furthermore, in response to your letter of 22 May 2007, we would like to provide the following information in addition to those submitted to you earlier vide our letter dated 24 May 2007 –

- (a) A copy of the minutes of the Special Board meeting held on 16 May 2007 Annex VII;
- (b) A list summarizing the similarities and differences of the problems on ASTRI's administration as identified by the Internal Audit of ASTRI and the Audit Commission (to be provided as soon as possible);
- (c) The duties and functions of the Head, Internal Audit and the Compliance Officer, the division of labour between the two posts and their line of reporting Annex VIII;
- (d) A summary table showing how the incentive payments were calculated for each of the 23 staff according to the formula approved by the Board Annex IX;
- (e) Regarding those 13 overdue final audited accounts mentioned in Table 15 in paragraph 4.41 of the Audit Report, seven of them were submitted to ITC as of February 2007. The remaining six accounts have been endorsed by ASTRI Audit Committee in May 2007 and will be submitted to ITC once they are endorsed by the Board in the coming Board meeting to be held in June 2007;
- (f) (i) Regarding the incorrect charging of project cost, the primary responsibility for controlling project costs rests with the project coordinator (PC). When a project progresses after project approval, the PC will provide the monthly budget data for charging the costs to the project, including manpower, material costs, etc, to the Accounting Department until the project is completed. For example, in the case of manpower costs, the PC will each month provide the Accounting Department with data concerning which staff members have worked how much time on a specific project (represented by project code). The Accounting Department will then calculate the manpower costs that should be charged to that project.

Similarly, in the case of material costs, the PC will request the Purchasing Department to purchase the required materials, and provide the project code for charging the concerned costs. The



Purchasing Department will, after checking with the Accounting Department on availability of funding, carry out the requisition order accordingly in accordance with established procurement procedures. When the materials are delivered, the R&D user Department/PC will certify receipt; Accounting Department then makes payment and charges the cost to the concerned project.

The Accounting Department prepares a monthly statement on the expenditures for each project for inspection by the Planning Department and the relevant PC. The PC, after checking whether the monthly spending pattern as set out in the monthly statement is in line with the budget and the milestones set for the project, will endorse all expenditure items stated in the monthly statement. Upon completion of each project, the PC will prepare a final report setting out the results of the projects and the expenditure incurred during the project period which will be submitted to ASTRI Technology Committee for endorsement and ITC for approval.

For the five projects mentioned in paragraph 5.9 of the Audit Report, they were under the same core technology platform as well as the same key technology initiative. The projects were undertaken by the same group of R&D staff, some of whom were working on more than one of the projects simultaneously. The concerned PC had charged the manpower costs to the wrong projects, partly because of the lack of an integrated computerized human resource system for the R&D team to record the time spent on each project on a real time basis, so that any erroneous entries could be identified readily. The mistakes were purely inadvertent ones.

(ii) The projects referred to in para. 5.9(c) of the Audit report are Project V and Project R. Both projects are under the same core technology platform (i.e. Digital Home Technology).

When a requisition for materials for Project V was made, the requisition order submitted by the R&D team contained the item name "Home Media Centre Personal Video Recorder" and specification such as "Printed Circuit Board" which were similar to equipment for both Projects V and R, and thus causing confusion. The Accounting Department was not aware of the wrong information in the requisition order form which was endorsed by the PC and had charged the material cost in question to the project account of project R.



ASTRI management is now correcting the concerned accounting records and financial reports. ASTRI management has also reminded the R&D teams and PCs to ensure that all expenditure items are accurately and properly charged to the correct project, and that Accounting Department should seek clarification from the R&D teams and PCs whenever there is any doubt on which project should be charged.

- (iii) ASTRI management has taken the following measures to ensure that approved funding of a project will only be used to cover the expenditures of that specific projects –
- R&D teams and PCs have been reminded that it is their responsibilities to ensure that all expenditure items are accurately and properly charged to the correct project, and that correct project codes should be clearly stated in all material requisitions and manpower charging forms;
- PCs have been reminded that they should ensure that expenses should only be used for the relevant projects, and they should exercise due diligence in charging the expenses to the relevant accounts
- the Accounting Department has also reminded the PC the importance of checking the accuracy of the expenses before their endorsement of the monthly statements;
- the Planning Department will also check the reasonableness and accuracy on the monthly statements issued by the Accounting Department;
- ASTRI is planning to implement a computerized and integrated HR and project management information system within this year and is studying different solutions on Enterprise Resource Planning, HR and project management systems. With the new system, the R&D team can record their time sheets into the system on a real time basis, thus allowing the PC to review and endorse them in a timely manner. The Accounting Department will then be able to work out the monthly statement based on the manpower data directly extracted from the same database and the HR and Planning Departments can review the manpower plan directly from the system on a real time basis. This should help ensure that the manpower cost is accurately and properly charged to the correct account.
- (g) On the engagement of feng shui consultants, our records did not show who decided or the criteria for deciding which feng shui consultants were to be invited for giving quotations for each of the



three procurements. Our procurement procedures require that more than one quotation is required for single purchase not exceeding HK\$10,000 and at least three quotations are required for any purchase with the value over HK\$50,000 but below HK\$1,000,000. While there is no further requirement on how or from whom the quotes should be obtained, we would, to ensure fairness, expect that the quotes are obtained in such a way that they are not from related parties. In this connection, you may wish to note that, to safeguard against potential conflict of interest, our employees are required under the Code of Conduct to declare to the Chief Executive Officer if they are called upon to deal with matters which may give rise to a conflict of interest with ASTRI.

Please note that Annexes I to VII and Annex IX are provided on the request of the PAC, on the understanding that they will be used solely for the purposes of the PAC discharging its functions. We would like to request that the confidentiality of the documents be observed and that the information provided will not be published.

Yours sincerely,

(Victor Chin) for Chairman

Board of Directors

c.c. Secretary for Commerce, Industry and Technology (Attn: Mr Joseph W P Wong)

Permanent Secretary for Commerce, Industry and Technology (Communications and Technology)

(Attn: Mr Francis Ho)

Commissioner for Innovation and Technology

(Attn: Mr Anthony S K Wong)

Secretary for Financial Services and the Treasury

(Attn: Miss Amy Tse)

Director of Audit (Attn: Mr Tony Ng)

*Note by Clerk, PAC: Annexes I to VII and IX not attached.

Duties and Functions of the Head of Internal Audit and the Compliance Officer

The primary responsibilities of Head of Internal Audit and Compliance Officer are as follows --

• Head of Internal Audit

- reviewing of accounting systems and related internal controls;
- examination of financial and operating information for management, including detailed testing of transactions and balances;
- reviewing of the economy, efficiency and effectiveness of operations, and of the functioning of non-financial controls;
- reviewing of the implementation of corporate policies, plans and procedures;
 and
- undertaking other special investigations directed by the Board.

Compliance Officer

- ensuring that the Board, through the Audit Committee, is fully kept informed of the parameters within which ASTRI should operate;
- ensuring that ASTRI follows all relevant procedures; and
- advising on, and assisting the Board in implementing procedures to ensure that the Company complies with all applicable regulations, guidelines and relevant statements of best practices.

On the line of responsibility, the Head of Internal Audit and the Compliance Officer should report separately to the Audit Committee as reflected in the new organization structure of ASTRI that was submitted to the PAC on 18 May 2007.