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31 May 2011

Ms Miranda HON
Clerk to Public Accounts Committee
Legislative Council
8/F Murray Road Multi-storey Carpark Building
Hong Kong
(Fax No.: 2840 0716)

Dear Ms Hon,

**The Director of Audit's Report on the
results of value for money audits (Report No. 56)**

Hong Kong 2009 East Asian Games (Chapter 5)

I refer to your letter of 25 May 2011 requesting further information on the source of funding for the legacy project and would like to provide relevant information as follows –

- (a) The \$10 million sponsorship received from Sponsor B on 22 January 2010 was to support the East Asian Games (EAG) generally and was made without reference to any designated use or specific conditions.
- (b) & (c) Sponsor B made two major donations to the EAG Company. The first one, amounting to about \$13 million, was pledged in early 2009 for specific EAG activities. The second one, amounting to \$10 million, was pledged in November 2009 without reference to any designated use. The second donation did not form a part of nor was it in any way related to the first one. The payment of the second donation was eventually received on 22 January 2010. It is not uncommon for sponsors to pledge a donation before an event is held and to make the actual payment afterwards.

- (d) With regard to the correspondence on the legacy project in May and June 2010: in May 2010, the Leisure and Cultural Services Department (LCSD) wrote to the Financial Services and the Treasury Bureau (FSTB) to propose that the EAG Company should be allowed to use its unallocated balance to fund two legacy projects. In response to an oral enquiry from FSTB, LCSD replied via an email that the Company had received some substantial “last-minute” donations, including the \$10 million donation from Sponsor A for enhancing the opening ceremony. This was cited as an example of a substantial “last-minute” donation secured by the Company, in support of LCSD’s point that a large proportion of the unallocated balance was attributable to such donations. LCSD did not give FSTB an exhaustive list of the last-minute donations received by the Company. To our understanding, the reference to Sponsor A in the reply from FSTB to LCSD was made to help illustrate the general principles that: *“if all (or part) of the unallocated balance of \$20 million can be attributed to community/commercial sponsorship received by the EAG Company, depending on the sponsorship terms, one could argue that the Government may not necessarily have the first claim on the balance (or that part of it)”* (paragraph 4 of Appendix V to Annex D of our previous reply to you). We have confirmed the above understanding with FSTB prior to issuing this letter. LCSD and FSTB did not discuss the specific source of the funding that was proposed for implementing the legacy projects.

As regards the position of the EAG Company: the Company initially took the view that the unallocated balance was the result of the combined efforts of all concerned to minimise expenditure and generate income, hence the final \$21.5 million unallocated balance should not be specifically attributed to individual donations. However, on the advice of the Administration, the Company accepted the general principles relating to the use of the unallocated balance and identified a \$10 million donation that met the principles stipulated by the Government relating to the allocation of funding for a legacy project.

When commenting on the relevant parts of the draft Audit report in February 2011, the former Chief Executive Officer (CEO) of the EAG Company was stating the Company’s initial position that the unallocated balance should not be attributed to one single sponsor. He was aware of the advice of the Administration regarding the use

of the unallocated balance on the legacy projects, and had implemented the projects having due regard to the principles concerned.

Our discussion with the Audit Commission on this area of the draft Audit report focused primarily on the rationale for allowing the EAG Company to use part of the unallocated balance on the two legacy projects; and on whether such use was permissible under the Tripartite Agreement. In February 2011, the former CEO of the EAG Company pointed out to the Audit Commission that the donation from Sponsor A had been used to enhance the opening ceremony. Neither LCS D nor the CEO were asked to clarify further the specific source of funding for the legacy projects.

As the Audit Commission's value-for-money study was conducted more than a year after the EAG was held, the EAG Company had ceased operation and no longer had any working staff. It should be appreciated that it was not always possible in the circumstances for the Administration, which was not directly responsible for organising the EAG, to provide detailed facts and figures within a tight timeframe and to trace the reasons behind some of the decisions taken by the Company. In these circumstances, it is possible that comments given by LCS D did not cover in full each and every aspect of the various issues raised by the Audit Commission.

As requested, the full text of the minute submitted by the Director of Leisure and Cultural Services to the Secretary for Home Affairs on 5 May 2010 is attached at **Annex**.

Yours sincerely,



(Benjamin Mok)
for Secretary for Home Affairs

c.c. Director of Leisure and Cultural Services (fax no. 2606 1824)
Secretary for Financial Services and the Treasury (fax no. 2147 5239)
Director of Audit (fax no. 2583 9063)

Full Text of the LCSD's minute submitted to SHA on 5 May 2010

M.1

**SHA
via PSHA
DS(HA)2**

**Disposal of Surplus Fund and Properties from
The Hong Kong 2009 East Asian Games (EAG)**

PROBLEM

The EAG Company will have a surplus of \$20M. We need to consider how to dispose of the surplus in a proper and meaningful manner.

RECOMMENDATION

2. It is recommended that the surplus and properties of the EAG Company be disposed of by:
 - (a) providing \$1M for the EAG legacy project at EAG-related venues;
 - (b) donating \$19M to the Hong Kong Athletes Career and Education Programme (HKACEP) and/or the Hong Kong Athlete Fund (HKAF) for the long-term benefits of Hong Kong athletes and the creation of a EAG legacy; and
 - (c) transferring the properties (office furniture and equipment) to LCSD.

JUSTIFICATION

The Surplus

3. The EAG has concluded successfully last December and the EAG Company (the Company) has been finalising its account. It is anticipated that

there will be a surplus of about HK\$20M if all the money receivable is duly received. The latest draft income and expenditure statement of the Company as at 31 March 2010 is at Annex A. Furthermore, the Company has procured office furniture and equipment (Annex B) which will be left behind upon its winding up.

4. Although the Company had reviewed and revised the budget on a continuous basis before and throughout the Games, a number of factors, which were not fully within the Company's control, have attributed to the higher than expected surplus. These include:

- (a) **Satisfactory ticket sales** – over 70% of the tickets were sold (80% of the education tickets purchased by [*sponsor's name has been deleted*] were included) and this had resulted in \$3M additional income (as compared to the original estimate) for the Company;
- (b) **Last-minute sponsorship** - sponsorship in kind including courier services for doping samples from Hong Kong to Beijing and supplies for sports equipment for various competitions were finalised at a very late stage, thus contributing to savings of around \$3M.
- (c) **Lower turnout of participants** – the actual number of participants (totalling 3,200 athletes, team officials and VIPs) in EAG, which was finalised and available only in late November 2009, was lower than the Company's original estimate (3,900). As a result, the expenditure on catering, accommodation, VIP hospitality, competition events, etc has reduced by around \$9M; and
- (d) **Other cost savings** – the Company had succeeded in negotiating with some of its contractors/service providers to lower the contract prices, notably in transportation and production costs of the opening ceremony, which has resulted in \$4M savings.

5. The relatively large surplus of EAG is a combined result of the concerted efforts of all to contain costs, the smaller number of participants as well as the better than expected ticket sales and sponsorship. While some may comment that the Company had been too prudent in planning its budget and hence resulted in certain inadequacies, we believe that the surplus should be defensible, especially if we are able to put it into good and meaningful use.

(a) Disposal of the Surplus

6. We have considered various ways to dispose of the surplus having regard to the Tripartite Agreement for 2009 EAG signed among the Government, the EAG Company and the Sports Federation and Olympic

Committee of Hong Kong, China (SF&OC), as well as the Memorandum of Articles and Association (MAA) of the Company. The justifications for our recommendations are as follows:

(i) EAG legacy projects

7. To commemorate Hong Kong hosting the 5th EAG, we propose to install commemorative plaques at 19 EAG-related venues owned by LCSD, including 16 competition venues and three other venues, namely the Kowloon Park Piazza, the Olympic Square in Hong Kong Park and the Hong Kong Cultural Centre Piazza where the 100-day countdown cum torch relay, the flag raising ceremony and the opening ceremony was held respectively. The Company is arranging for the design of these commemorative plaques which will display the relevant EAG mascots and events, as well as the dates on which the events were held at that particular venue. This legacy project is estimated to cost about \$1M. We aim to complete the project by late June 2010 so that the payment can be effected before the Company winds up.

(ii) Donation to the Hong Kong Athletes Career and Education Programme and Hong Kong Athletes Fund

8. To further the spirit of the EAG and having regard to Clause 3(13) of the object of the MAA which states that the Company may “*subscribe or guarantee money for charitable/religious or educational objects, and to promote, contribute to or assist financially or otherwise any fund for any charitable purposes*”, we propose that the remaining surplus (around \$19M) should be used to benefit Hong Kong’s athletes directly. In this connection, two possible funds, both with the objective of helping Hong Kong’s serving and retired athletes to pursue excellence in their sports and to support their career and educational development, have been identified for the purpose of the donation. They are the Hong Kong Athletes Career and Education Programme (HKACEP) and the Hong Kong Athletes Fund (HKAF).

9. The HKACEP is operated by the SF&OC. Through supporting top athletes’ career and education development, the Programme aims to nurture well respected world class sports talents to be the role models of youth and to honour their sports achievements and dedication to Hong Kong’s sports success. The HKAF, operated by the Hong Kong Sports Institute Limited (HKSI), aims to provide grants for educational and other academic training to individual athletes to enable them to pursue excellence in their chosen sports and provide them with the opportunity to develop alternative careers upon retirement from sports. Information on the HKACEP and the HKAF is at Annex C and D respectively.

10. The donation of EAG surplus to either the HKACEP or HKAF or both will be a welcomed addition to the on-going efforts to support Hong Kong athletes' career and education development, a major area of concern of the sports community. To highlight the outstanding achievements of Hong Kong's athletes in the 5th EAG, we intend to explore with SF&OC and HKSI the possibility of setting up an EAG scholarship or a sub-fund under HKACEP and/or HKAF so as to benefit the EAG medallists/athletes (including participants in future EAGs) more directly and to create an intangible but long-lasting legacy for the 5th EAG. We believe that this proposal will be welcomed by the sports sector and will most likely be supported by the Company's Board of Directors.

Alternatives considered

(i) Returning the donation to [sponsor's name has been deleted]

11. We have considered the suggestion of returning to *[sponsor's name has been deleted]* its donation of *[amount of sponsorship has been deleted]*. Although the *[amount of sponsorship has been deleted]* had been claimed and banked in by the Company, the *[sponsor's name has been deleted]* advised that there is no technical hurdle barring the return of the donation. However, we are concerned that the arrangement will attract queries or even criticisms from other EAG sponsors, in particular the *[sponsor's name has been deleted]* which is also a major sponsor of the EAG using its charity funds. They may ask for similar treatment so that they could redeploy the funding to other charitable purposes. In view of the read-across implications, we do not recommend this option. We also anticipate that the Company's Board of Directors (among them is *[sponsor's name has been deleted]*) will not support such proposal.

(ii) Returning the surplus to Government

12. According to the Tripartite Agreement for the 2009 EAG at Annex E (Clause 16), surplus fund from EAG, if any, up to the total amount of Government subsidy provided (\$123 million) and hiring charges waived, shall be returned to the Government. However, the meaning of "surplus" is not clearly defined and is subject to interpretation. If the Government subsidy has been used up in accordance with the Company's object as set out in its MAA and expressed as expenditure items in the Company's account, then only the net surplus upon the winding up of the Company and after settlement of all its debts and liabilities should be returned to the Government. As mentioned in paragraph 8 above and as confirmed by the Company's legal advisor, donating the EAG surplus to funds that will benefit athletes falls within Clause 3(13) of the MAA and could be a legitimate expenditure item.

(b) Disposal of office furniture and equipment

13. As regards the Company's office furniture and equipment, we have considered two options, namely, to dispose them through auction or to give them to LCSD. We do not recommend the auction route as the Company has to incur costs for auction and the items auctioned would unlikely attract good value. Instead, we recommend that they be given away to LCSD upon the winding up of the Company. Not only will this save the Company's administrative cost (the expenditure will otherwise be donated to the athlete funds), the office furniture and equipment could also be put to good use by LCSD as it has to relocate its existing offices in the Hong Kong Park to the Company's office at the HK Squash Centre (HKSC) shortly (see paragraph 14).

14. The Company's office in the HKSC was converted from six squash courts. There is at present adequate supply of squash courts all over the territory. Utilization statistics and other relevant information revealed that the closure of the six squash courts in the past few years has not affected adversely the development of the sport. Moreover, about \$5M had been spent on converting the squash courts into office and the estimated cost for reinstatement obtained from ArchSD is in the region of \$5M. To require the Company to reinstate its office into squash courts will mean a \$5M reduction in the donation to the athlete funds. These factors, coupled with LCSD's genuine need for office space to accommodate the expanded Tree Teams and to relocate its HK Park Management Office currently housed in the Rawlinson House (a Grade 1 historic building in HK Park to be taken over by the Commissioner for Heritage), make the reinstatement of the office into squash courts unnecessary and unjustified. We have sought the views of Hong Kong Squash (the National Sports Association) on our intention not to reinstate the EAG office to squash courts. We do not expect strong objection from them as we have allowed them the continual use of 12 squash courts at the Cornwall Street Squash and Table Tennis Centre even after the return of the elite training base to the HKSI Fo Tan campus early this year.

Way Forward

15. Subject to your endorsement of the recommendations set out in paragraph 2 above, we will sound out FSTB informally on the proposed arrangements. Thereafter, we will assist the Company to seek the Board's approval of the recommendations in May 2010 so that the Company can proceed to appoint a liquidator for the winding up in June 2010.

DLCS
5.5.2010

****Note by Clerk, PAC: Annexes not attached.***